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OMZ (Uralmash-Izhora Group)

International Financial Reporting Standards  
Consolidated Financial Statements

31 December 2004

CAO

**OMZ**

~~United Heavy Machinery~~

## Contents

|   |   |
|---|---|
| Auditor's report .....                            | 1 |
| Consolidated Balance Sheet .....                  | 2 |
| Consolidated Income Statement .....               | 3 |
| Consolidated Cash Flow Statement .....            | 4 |
| Consolidated Statement of Changes in Equity ..... | 4 |

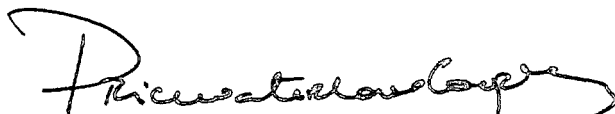
## Notes to the Financial Statements

|  |    |
|--|----|
| 1. The OMZ Group and its operations .....                  | 5  |
| 2. Financial position .....                                | 5  |
| 3. Basis of presentation of the financial statements ..... | 5  |
| 4. Significant accounting policies .....                   | 9  |
| 5. Segment information .....                               | 15 |
| 6. Business combinations .....                             | 19 |
| 7. Balances and transactions with related parties .....    | 21 |
| 8. Cash and cash equivalents .....                         | 24 |
| 9. Trade and other receivables .....                       | 24 |
| 10. Inventories .....                                      | 25 |
| 11. Other current financial assets .....                   | 25 |
| 12. Property, plant and equipment .....                    | 26 |
| 13. Deposit on investments .....                           | 27 |
| 14. Intangible assets .....                                | 27 |
| 15. Non-current financial assets .....                     | 28 |
| 16. Negative goodwill .....                                | 29 |
| 17. Trade and other accounts payable .....                 | 29 |
| 18. Borrowings .....                                       | 30 |
| 19. Long-term taxes payable .....                          | 32 |
| 20. Other long-term liabilities .....                      | 33 |
| 21. Equity .....   | 33 |
| 22. Construction contracts .....                           | 34 |
| 23. Cost of sales .....                                    | 35 |
| 24. Selling expenses .....                                 | 35 |
| 25. General and administrative expenses .....              | 35 |
| 26. Other operating income and expenses .....              | 36 |
| 27. Finance income/(expense) -net .....                    | 36 |
| 28. Income tax .....                                       | 36 |
| 29. Provisions for liabilities and charges .....           | 38 |
| 30. Contingencies, commitments and operating risks .....   | 39 |
| 31. Earnings per share .....                               | 41 |
| 32. Principal subsidiaries .....                           | 42 |
| 33. Financial risk management .....                        | 43 |
| 34. Post balance sheet events .....                        | 43 |

AUDITORS' REPORT

To the Shareholders of OAO OMZ (Uralmash-Izhora Group)

- 1 We have audited the accompanying consolidated balance sheet of OAO OMZ and its subsidiaries (the Group) as of 31 December 2004 and the related consolidated statements of income, of cash flow and of changes in shareholders' equity for the year then ended. These financial statements, as set out on pages 1 to 43, are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audit.
- 2 We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.
- 3 In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2004, and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.



29 April 2005  
Moscow, Russian Federation

OMZ

**Consolidated Balance Sheet at 31 December 2004**  
(in thousands of US dollars except for per share amounts)

OMZ

|  |      | As at 31 December     |                |                         |                |
|--|------|-----------------------|----------------|-------------------------|----------------|
|  |      | Continuing operations |                | Discontinued operations | Entity         |
|  | Note | 2004                  | 2003           | 2003                    | 2003           |
| <b>ASSETS</b>  |      |                       |                |                         |                |
| <b>Current assets:</b>   |      |                       |                |                         |                |
| Cash and cash equivalents  | 8    | 24,393                | 8,049          | 16,012                  | 24,061         |
| Trade and other receivables  | 9    | 443,236               | 281,868        | 115,939                 | 356,138        |
| Inventories  | 10   | 145,295               | 132,782        | 61,841                  | 194,623        |
| Other current financial assets   | 11   | 3,512                 | 4,780          | 6,385                   | 8,253          |
| <b>Total current assets</b>  |      | <b>616,436</b>        | <b>427,479</b> | <b>200,177</b>          | <b>583,075</b> |
| <b>Non-current assets:</b>   |      |                       |                |                         |                |
| Property, plant and equipment  | 12   | 201,298               | 133,569        | 80,355                  | 213,924        |
| Deposit on investments   | 13   | -                     | 5,031          | 10                      | 5,041          |
| Intangible assets  | 14   | 41,951                | 9,805          | 4,409                   | 14,214         |
| Negative goodwill  | 16   | (22,379)              | (26,977)       | (15,519)                | (42,496)       |
| Deferred tax asset   | 28   | 7,071                 | 8,895          | 2,274                   | 11,169         |
| Non-current financial assets   | 15   | 56,667                | 6,990          | 42,861                  | 49,851         |
| Investments in discontinued operations                                   | 3    | -                     | 84,754         | -                       | -              |
| <b>Total non-current assets</b>  |      | <b>284,608</b>        | <b>222,067</b> | <b>114,390</b>          | <b>251,703</b> |
| <b>Total assets</b>  |      | <b>901,044</b>        | <b>649,546</b> | <b>314,567</b>          | <b>834,778</b> |
| <b>LIABILITIES</b>   |      |                       |                |                         |                |
| <b>Current liabilities:</b>  |      |                       |                |                         |                |
| Trade and other payables   | 17   | 461,892               | 254,146        | 100,054                 | 323,496        |
| Short-term borrowings  | 18   | 122,045               | 195,036        | 24,228                  | 205,387        |
| <b>Total current liabilities</b>   |      | <b>583,937</b>        | <b>449,182</b> | <b>124,282</b>          | <b>528,883</b> |
| <b>Non-current liabilities:</b>  |      |                       |                |                         |                |
| Long-term borrowings   | 18   | 97,438                | 43,503         | 183                     | 43,686         |
| Long-term taxes payable  | 19   | 10,447                | 27,739         | 2,585                   | 30,324         |
| Deferred tax liability   | 28   | 29,126                | 8,121          | 14,227                  | 22,348         |
| Other long-term liabilities  | 20   | 8,877                 | 1,905          | 37,610                  | 39,515         |
| <b>Total non-current liabilities</b>                                     |      | <b>145,888</b>        | <b>81,268</b>  | <b>54,605</b>           | <b>135,873</b> |
| <b>Total liabilities</b>   |      | <b>729,825</b>        | <b>530,450</b> | <b>178,887</b>          | <b>664,756</b> |
| <b>EQUITY</b>  |      |                       |                |                         |                |
| <b>Equity and reserves attributable to the Company's equity holders:</b> |      |                       |                |                         |                |
| Share capital  | 21   | 419                   | 394            | 86,568                  | 394            |
| Share premium  |      | 104,081               | 96,487         | -                       | 96,487         |
| Treasury shares  | 21   | (44,507)              | (33)           | -                       | (33)           |
| Hedging reserve  | 21   | 812                   | -              | -                       | -              |
| Currency translation reserve   |      | 14,773                | 388            | 935                     | 3,137          |
| Retained earnings (deficit)  |      | 70,251                | (1,325)        | 6,624                   | 5,299          |
|  |      | <b>145,829</b>        | <b>95,911</b>  | <b>94,127</b>           | <b>105,284</b> |
| <b>Minority interest</b>   |      | <b>25,390</b>         | <b>23,185</b>  | <b>41,553</b>           | <b>64,738</b>  |
| <b>Total equity</b>  |      | <b>171,219</b>        | <b>119,096</b> | <b>135,680</b>          | <b>170,022</b> |
| <b>Total liabilities and equity</b>                                      |      | <b>901,044</b>        | <b>649,546</b> | <b>314,567</b>          | <b>834,778</b> |

General Director  
Lipsky S.V.

Chief Financial Officer  
Filatov S.N.

**OMZ****Consolidated Income Statement for the year, ended 31 December 2004***(in thousands of US dollars unless otherwise stated)***OMZ**

|  | Note | 2004                  |                         |                | 2003                  |                         |                |
|--|------|-----------------------|-------------------------|----------------|-----------------------|-------------------------|----------------|
|  |      | Continuing operations | Discontinued operations | Entity         | Continuing operations | Discontinued operations | Entity         |
| Sales  |      | 523,797               | 137,594                 | 661,391        | 340,109               | 206,126                 | 546,235        |
| Cost of sales  | 23   | (421,783)             | (100,007)               | (521,790)      | (235,315)             | (157,664)               | (392,979)      |
| <b>Gross profit</b>  |      | <b>102,014</b>        | <b>37,587</b>           | <b>139,601</b> | <b>104,794</b>        | <b>48,462</b>           | <b>153,256</b> |
| Selling expenses   | 24   | (21,158)              | (2,613)                 | (23,771)       | (12,193)              | (2,782)                 | (14,975)       |
| General and administrative expenses  | 25   | (83,083)              | (19,359)                | (102,442)      | (85,762)              | (30,663)                | (116,425)      |
| Other operating income and expenses  | 26   | 13,651                | 301                     | 13,952         | 24,958                | (6,417)                 | 18,541         |
| <b>Operating profit before negative goodwill</b>                                     |      | <b>11,424</b>         | <b>15,916</b>           | <b>27,340</b>  | <b>31,797</b>         | <b>8,600</b>            | <b>40,397</b>  |
| Negative goodwill  | 6    | 113,907               | -                       | 113,907        | -                     | -                       | -              |
| <b>Operating profit</b>  |      | <b>125,331</b>        | <b>15,916</b>           | <b>141,247</b> | <b>31,797</b>         | <b>8,600</b>            | <b>40,397</b>  |
| Finance income/(expense) – net   | 27   | 2,390                 | (16)                    | 2,374          | (12,562)              | 4,054                   | (8,508)        |
| Loss from equity accounted investments   | 7    | -                     | -                       | -              | (4,707)               | (256)                   | (4,963)        |
| <b>Profit before taxation and sale of discontinued operations</b>                    |      | <b>127,721</b>        | <b>15,900</b>           | <b>143,621</b> | <b>14,528</b>         | <b>12,398</b>           | <b>26,926</b>  |
| Income tax benefit (expense)   | 28   | (12,724)              | (7,219)                 | (19,943)       | 1,882                 | (6,120)                 | (4,238)        |
| <b>Profit for the year before loss from sale of discontinued operations</b>          |      | <b>114,997</b>        | <b>8,681</b>            | <b>123,678</b> | <b>16,410</b>         | <b>6,278</b>            | <b>22,688</b>  |
| Loss from sale of discontinued operations  | 7    | (53,975)              | -                       | (53,975)       | -                     | -                       | -              |
| <b>Profit for the year</b>   |      | <b>61,022</b>         | <b>8,681</b>            | <b>69,703</b>  | <b>16,410</b>         | <b>6,278</b>            | <b>22,688</b>  |
| <b>Attributable to:</b>  |      |                       |                         |                |                       |                         |                |
| Equity holders of the Company  |      | 59,116                | 4,398                   | 63,514         | 20,246                | 4,737                   | 24,983         |
| Minority interest  |      | 1,906                 | 4,283                   | 6,189          | (3,836)               | 1,541                   | (2,295)        |
|  |      | <b>61,022</b>         | <b>8,681</b>            | <b>69,703</b>  | <b>16,410</b>         | <b>6,278</b>            | <b>22,688</b>  |
| Earnings per share attributable to the equity holders of the Company (in US dollars) |      |                       |                         |                |                       |                         |                |
| - basic  | 31   | 1.85                  | 0.14                    | 1.99           | 0.64                  | 0.14                    | 0.78           |
| - diluted  | 31   | 1.82                  | 0.13                    | 1.95           | 0.61                  | 0.14                    | 0.75           |

**OMZ****Consolidated Cash Flow Statement for the year ended 31 December 2004***(in thousands of US dollars unless otherwise stated)***OMZ**

|  |       | 2004                  |                         |                 | 2003                  |                         |                 |
|--|-------|-----------------------|-------------------------|-----------------|-----------------------|-------------------------|-----------------|
|  | Note  | Continuing operations | Discontinued operations | Entity          | Continuing operations | Discontinued operations | Entity          |
| <b>Cash flows from operating activities</b>  |       |                       |                         |                 |                       |                         |                 |
| Profit before taxation and sale of discontinued operations                                 |       | 127,721               | 15,900                  | 143,621         | 14,528                | 12,398                  | 26,926          |
| Adjustments for:   |       |                       |                         |                 |                       |                         |                 |
| Depreciation and amortization  | 23,25 | 17,713                | 5,544                   | 23,257          | 7,776                 | 8,598                   | 16,374          |
| Change in provisions for impairment and other provisions                                   | 26    | 25,070                | (572)                   | 24,498          | (1,865)               | 5,615                   | 3,750           |
| Gain on sale of non-core business units  | 26    | (21,352)              | (12)                    | (21,364)        | (14,666)              | -                       | (14,666)        |
| Negative goodwill, recognized in profit  | 6     | (113,907)             | -                       | (113,907)       | -                     | -                       | -               |
| Gain from disposal of property, plant and equipment  | 26    | (6,831)               | (263)                   | (7,094)         | (3,149)               | 209                     | (2,940)         |
| Gain on release from government financing and tax penalties                                | 26    | (9,613)               | 159                     | (9,454)         | (2,738)               | (356)                   | (3,094)         |
| Net finance cost adjusted for foreign exchange differences                                 | 27    | 19,377                | 1,311                   | 20,688          | 20,890                | 455                     | 21,345          |
| Loss from equity accounted investments   |       | -                     | (161)                   | (161)           | 4,707                 | 256                     | 4,963           |
| Unrealized foreign exchange effect on non-operating items                                  |       | (9,806)               | (1,004)                 | (10,810)        | (3,920)               | (860)                   | (4,780)         |
| Adjustments for non-cash investing activities  | 21    | -                     | -                       | -               | 3,999                 | -                       | 3,999           |
| <b>Operating cash flows before working capital changes</b>                                 |       | <b>28,372</b>         | <b>20,902</b>           | <b>49,274</b>   | <b>25,562</b>         | <b>26,315</b>           | <b>51,877</b>   |
| Decrease (increase) in accounts receivable and prepayments                                 |       | (90,387)              | (32,919)                | (123,306)       | (95,981)              | (44,920)                | (140,901)       |
| Decrease (increase) in inventories   |       | 16,832                | (21,446)                | (4,614)         | (24,133)              | (11,448)                | (35,581)        |
| Increase (decrease) in trade and other accounts payable                                    |       | 62,717                | 16,701                  | 79,418          | 44,616                | 8,002                   | 52,618          |
| <b>Cash provided from (used in) operations</b>   |       | <b>17,534</b>         | <b>(16,762)</b>         | <b>772</b>      | <b>(49,936)</b>       | <b>(22,051)</b>         | <b>(71,987)</b> |
| Income taxes paid  |       | (1,082)               | (3,171)                 | (4,253)         | (2,735)               | (1,668)                 | (4,403)         |
| <b>Net cash provided from (used in) operating activities</b>                               |       | <b>16,452</b>         | <b>(19,933)</b>         | <b>(3,481)</b>  | <b>(52,671)</b>       | <b>(23,719)</b>         | <b>(76,390)</b> |
| <b>Cash flows from investing activities:</b>   |       |                       |                         |                 |                       |                         |                 |
| Proceeds from sale of non-core business units, including discontinued operations           |       | 58,946                | 4,876                   | 63,822          | 14,664                | -                       | 14,664          |
| Cash of discontinued operations at the date of disposal                                    |       | -                     | (17,125)                | (17,125)        |                       |                         |                 |
| Purchases of property, plant and equipment, intangibles                                    |       | (6,840)               | (4,667)                 | (11,507)        | (13,292)              | (3,958)                 | (17,250)        |
| Proceeds from the sale of property, plant and equipment, intangibles and development costs |       | 7,453                 | 396                     | 7,849           | 5,427                 | 174                     | 5,601           |
| Net sale/(purchases) of financial assets   |       | (6,039)               | (337)                   | (6,376)         | 744                   | 1,604                   | 2,348           |
| Deposit on investments   | 13    | -                     | -                       | -               | (5,041)               | -                       | (5,041)         |
| Business combinations  | 6     | 5,819                 | -                       | 5,819           | (32,290)              | 10,902                  | (21,388)        |
| Purchase of associates   |       | -                     | -                       | -               | (4,963)               | -                       | (4,963)         |
| Net change in deposits   |       | 4,744                 | 1,759                   | 6,503           | (1,937)               | 1,492                   | (445)           |
| Interest received  |       | 2,477                 | 201                     | 2,678           | 252                   | 1,750                   | 2,002           |
| Net proceeds from loans issued   |       | 9,567                 | -                       | 9,567           | (7,042)               | (7,211)                 | (14,253)        |
| <b>Net cash provided from (used in) investing activities</b>                               |       | <b>76,127</b>         | <b>(14,897)</b>         | <b>61,230</b>   | <b>(43,478)</b>       | <b>4,753</b>            | <b>(38,725)</b> |
| <b>Cash flows from financing activities:</b>   |       |                       |                         |                 |                       |                         |                 |
| Proceeds from borrowings   |       | 144,043               | 33,182                  | 177,225         | 110,920               | 27,520                  | 138,440         |
| Repayment of borrowings  |       | (149,769)             | (12,392)                | (162,161)       | (4,199)               | -                       | (4,199)         |
| Repayment of long-term taxes payable   |       | (5,324)               | (688)                   | (6,012)         | (7,035)               | -                       | (7,035)         |
| Sale/(purchase) of treasury shares   |       | (42,500)              | -                       | (42,500)        | 418                   | -                       | 418             |
| Interest paid  |       | (26,996)              | (1,513)                 | (28,509)        | (19,171)              | (2,073)                 | (21,244)        |
| Dividends paid   |       | (1)                   | -                       | (1)             | (1)                   | -                       | (1)             |
| <b>Net cash (used in) provided from financing activities</b>                               |       | <b>(80,547)</b>       | <b>18,589</b>           | <b>(61,958)</b> | <b>80,932</b>         | <b>25,447</b>           | <b>106,379</b>  |
| Effect of exchange rate changes  |       | 4,312                 | 229                     | 4,541           | 1,030                 | 911                     | 1,941           |
| <b>Net increase (decrease) in cash and cash equivalents</b>                                |       | <b>(16,244)</b>       | <b>(1,113)</b>          | <b>(17,357)</b> | <b>(1,107)</b>        | <b>(1,351)</b>          | <b>(2,458)</b>  |

OMZ

**Consolidated Statement of Changes in Equity for the year ended 31 December 2004**  
(in thousands of US dollars unless otherwise stated)

**OMZ**

|  | Note | Attributable to shareholders |                |                 |                 |                              | Minority interest | Total equity          |
|--|------|------------------------------|----------------|-----------------|-----------------|------------------------------|-------------------|-----------------------|
|  |      | Share capital                | Share premium  | Treasury shares | Hedging reserve | Currency translation reserve | Retained earnings |                       |
| <b>Balance at 31 December 2002</b>                                 |      | <b>366</b>                   | <b>83,662</b>  | <b>(38)</b>     | <b>-</b>        | <b>1,998</b>                 | <b>(18,244)</b>   | <b>64,369 132,113</b> |
| Currency translation   |      | 28                           | 6,615          | -               | -               | 1,139                        | (1,439)           | 4,977 11,320          |
| Net income/(expense) recognised directly in equity                 |      | 28                           | 6,615          | -               | -               | 1,139                        | (1,439)           | 4,977 11,320          |
| Profit for the year  |      | -                            | -              | -               | -               | -                            | 24,983            | (2,295) 22,688        |
| Total recognised income  |      | 28                           | 6,615          | -               | -               | 1,139                        | 23,544            | 2,682 34,008          |
| Employees share option scheme:                                     | 21   |                              |                |                 |                 |                              |                   |                       |
| - value of employees services                                      |      | -                            | 3,999          | -               | -               | -                            | -                 | - 3,999               |
| - proceeds from sale of treasury shares                            |      | -                            | 416            | 2               | -               | -                            | -                 | - 418                 |
| Dividends  |      | -                            | -              | -               | -               | -                            | (1)               | - (1)                 |
| Acquisition of additional shares in subsidiaries                   | 6    | -                            | 1,795          | 3               | -               | -                            | -                 | (7,753) (5,955)       |
| Disposal of subsidiaries   |      | -                            | -              | -               | -               | -                            | -                 | (459) (459)           |
| Business combinations  | 6    | -                            | -              | -               | -               | -                            | -                 | 5,899 5,899           |
| <b>Balance at 31 December 2003</b>                                 |      | <b>394</b>                   | <b>96,487</b>  | <b>(33)</b>     | <b>-</b>        | <b>3,137</b>                 | <b>5,299</b>      | <b>64,738 170,022</b> |
| Currency translation   |      | 25                           | 5,932          | (2,079)         | -               | 14,397                       | 1,439             | (2,174) 17,540        |
| Net income/(expense) recognised directly in equity                 |      | 25                           | 5,932          | (2,079)         | -               | 14,397                       | 1,439             | (2,174) 17,540        |
| Profit for the year  |      | -                            | -              | -               | -               | -                            | 63,514            | 6,189 69,703          |
| Total recognised income  |      | 25                           | 5,932          | (2,079)         | -               | 14,397                       | 64,953            | 4,015 87,243          |
| Disposal of non-core businesses, including discontinued operations | 7,26 | -                            | -              | -               | -               | (2,761)                      | -                 | (42,164) (44,925)     |
| Additional issue of shares   | 21   | -                            | 1,662          | -               | -               | -                            | -                 | - 1,662               |
| Employees share option scheme:                                     | 21   |                              |                |                 |                 |                              |                   |                       |
| - proceeds from sale of treasury shares                            |      | -                            | -              | 105             | -               | -                            | -                 | - 105                 |
| Purchase of treasury shares  | 21   | -                            | -              | (42,500)        | -               | -                            | -                 | - (42,500)            |
| Cash flow hedges, net of tax                                       | 33   | -                            | -              | -               | 812             | -                            | -                 | - 812                 |
| Acquisition of additional shares in subsidiaries                   | 6    | -                            | -              | -               | -               | -                            | -                 | (1,199) (1,199)       |
| Dividends  |      | -                            | -              | -               | -               | -                            | (1)               | - (1)                 |
| <b>Balance at 31 December 2004</b>                                 |      | <b>419</b>                   | <b>104,081</b> | <b>(44,507)</b> | <b>812</b>      | <b>14,773</b>                | <b>70,251</b>     | <b>25,390 171,219</b> |



## **1. The OMZ Group and its operations**

OAO OMZ and its subsidiaries ("OMZ" or "the Group") operate in four business segments comprising nuclear power plant equipment, speciality steels, machinery equipment manufacturing and mining equipment. The Group's manufacturing facilities are primarily based in Russia and the Czech Republic. The parent company, OAO OMZ ("the Company") was incorporated as an open joint stock company in Ekaterinburg, Russian Federation in 1996. OMZ's principal subsidiaries are disclosed in note 32. These are incorporated under the Laws of the Russian Federation and the Czech Republic.

In May 2004 the Group sold Morskie Neftegazovie Proekty ("MNP") comprising primarily OMZ's previous oil and gas equipment and shipbuilding segments for US\$50 million to its management (note 7). The financial results, assets and liabilities of the companies, included in the disposed segments, are disclosed in the Financial Statements separately as discontinued operations (note 3).

In July 2004 the Group acquired 100 percent of the shares in three companies (ŠKODA JS a.s. and ŠKODA STEEL (which includes ŠKODA HUTE s.r.o. and ŠKODA KOVARNY s.r.o.)) from ŠKODA HOLDING and Appian Group plc (note 6).

At 31 December 2004 the Group employed approximately 22,030 employees (December 31, 2003: 42,988). The decrease in number of employees was primarily due to the disposal of MNP.

## **2. Financial position**

A significant part of the Group's borrowings are short term in nature. At 31 December 2004 the Group had a total of \$219,483 of borrowings (2003: \$249,073) of which \$122,045 (2003: \$205,387) is payable within one year. In addition, as stated in Note 18 there are \$24,275 of long term bonds, which the company may have to repay during 2005 under certain conditions. The Group has a history of successfully refinancing or paying its debts and other liabilities as they fall due and management fully expect that this will continue through the foreseeable future based on the following factors:

- the Group's historical track record in refinancing its short term loans
- the fact, that the group experienced positive operating cash flows from continuing operations in 2004 of \$16,452
- the positive working capital position at 31 December 2004
- the possibilities of raising additional finance afforded by the 4,551 thousand ordinary shares held by the company in treasury
- the fact that based on current market prices of the bonds, referred to above management does not expect these to be redeemed during 2005
- the Group has unused credit facilities as set out in Note 18 .

## **3. Basis of presentation of the financial statements**

The consolidated financial statements of OMZ Group have been prepared in accordance with International Financial Reporting Standards (IFRS).

The Group companies maintain their accounting records in the respective currency and prepare their statutory financial statements in accordance with local regulations of accounting of the country in which the particular subsidiary is resident. The financial statements are based on the statutory records, with adjustments and reclassifications recorded for the purpose of fair presentation in accordance with IFRS.

### **3. Basis of presentation of the financial statements (continued)**

#### ***Early adoption of standards***

In 2003, the Group early adopted the standards below, which are relevant to its operations.

IAS 1 (revised 2003) Presentation of Financial Statements  
IAS 32 (revised 2003) Financial Instruments: Disclosure and Presentation  
IAS 39 (revised 2003) Financial Instruments: Recognition and Measurement  
IFRS 2 (issued 2004) Share-based Payments

In 2004, the Group early adopted the standards below, which are relevant to its operations.

IAS 2 (revised 2003) Inventories  
IAS 8 (revised 2003) Accounting Policies, Changes in Accounting Estimates and Errors  
IAS 10 (revised 2003) Events after the Balance Sheet Date  
IAS 16 (revised 2003) Property, Plant and Equipment  
IAS 21 (revised 2003) The Effects of Changes in Foreign Exchange Rates  
IAS 24 (revised 2003) Related Party Disclosures  
IAS 27 (revised 2003) Consolidated and Separate Financial Statements  
IAS 33 (revised 2003) Earnings per Share  
IAS 36 (revised 2004) Impairment of Assets  
IAS 38 (revised 2004) Intangible Assets

The early adoption of IAS 2, 8, 10, 16, 21, 24, 27, 33 and 38 did not result in substantial changes to the Group's accounting policies. In summary:

- IAS 2, 8, 10, 16, 27 and 33 had no material effect on the Group's policies.
- IAS 21 (revised 2003) had no material effect on the Group's policy. The functional currency of each of the consolidated entities has been re-evaluated based on the guidance to the revised standard.
- IAS 24 (revised 2003) has affected the identification of related parties and some other related party disclosures.
- The Group has reassessed the useful life of its intangible assets in accordance with the provision of IAS 38. No adjustment resulted from this reassessment.

The adoption of IAS 36 (revised 2004) resulted in a change in the accounting policy for goodwill. Until adoption of these standards, goodwill was assessed for an indication of impairment at each balance sheet date. After the year ended 31 December 2003, goodwill is tested annually for impairment, as well as when there is an indication of impairment.

All changes in the accounting policies have been made in accordance with the transition provisions in the respective standards.

There was no impact on opening retained earnings at 1 January 2004 from the adoption of the standards mentioned above.

#### ***Presentation of continuing operations and "Entity"***

During 2004 the Group sold a substantial part of its operations – the oil and gas equipment and shipbuilding business segments – to certain members of management. In order to provide more meaningful information in the financial statements, the income statements for 2004 and 2003 are presented as continuing and discontinued operations, the latter representing the results of the segments sold to the date of their disposal. The "Entity" column represents the results of the Group as a whole, including continuing and discontinued operations up to the date of the sale.

Similarly the balance sheet at 31 December 2003 is presented as continuing and discontinued operations. At 31 December 2004 the Group balance sheet is equal to the balance sheet of the continuing operations.

**3. Basis of presentation of the financial statements (continued)*****Presentation of continuing operations and "Entity" (continued)***

The following balances receivable or payable between continuing/discontinued operations are eliminated against each other in arriving at the Entity balance sheet:

|  | 2003           |
|--|----------------|
| <b>ASSETS</b>  |                |
| <b>Current assets:</b>   |                |
| Trade and other receivables from continuing operations                   | 13,086         |
| Trade and other receivables from discontinued operations                 | 28,583         |
| Other current financial assets from continuing operations                | 2,912          |
| <b>Total current assets</b>  | <b>44,581</b>  |
| <b>Non-current assets:</b>   |                |
| Investments of continuing operations in discontinued                     | 84,754         |
| <b>Total non-current assets</b>  | <b>84,754</b>  |
| <b>Total assets</b>  | <b>129,335</b> |
| <b>LIABILITIES</b>   |                |
| <b>Current liabilities:</b>  |                |
| Trade and other payables to continuing operations                        | 16,709         |
| Trade and other payables to discontinued operations                      | 13,995         |
| Short-term borrowings payable to continuing operations                   | 11,874         |
| Short-term borrowings payable to discontinued operations                 | 2,003          |
| <b>Total current liabilities</b>   | <b>44,581</b>  |
| <b>EQUITY</b>  |                |
| <b>Equity and reserves attributable to the Company's equity holders:</b> |                |
| Currency translation reserve of discontinued operations                  | (1,814)        |
| Share capital of discontinued operations                                 | 86,568         |
| <b>Total equity</b>  | <b>84,754</b>  |
| <b>Total liabilities and equity</b>                                      | <b>129,335</b> |

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below.

***Foreign currency translation***

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). For most of the Group's entities the functional currency is the Russian Rouble, except for those entities operating in the Czech Republic for which the functional currency is the Czech Koruna. As management considers that the US dollar is a more convenient currency for users of these consolidated financial statements, these consolidated financial statements are presented in US dollars - the Group's presentation currency.

Monetary assets and liabilities held by Group entities and denominated in foreign currencies at 31 December 2004 are translated into the Russian Rouble at the exchange rate prevailing at that date. Foreign currency transactions are accounted for at the exchange rate prevailing at the date of the transaction. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currency are recognised in the income statement.

The results and financial position of those Group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

### 3. Basis of presentation of the financial statements (continued)

#### *Foreign currency translation (continued)*

- (i) assets and liabilities in each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- (ii) income and expenses in each income statement presented are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- (iii) all resulting exchange differences are recognised as a currency translation reserve in equity.

At 31 December 2004, the official rates of exchange, as determined by the Central Bank of the Russian Federation, were US dollar (US\$) 1=RR 27.75 (December 31, 2003 USD1=RR 29.45) and Czech Koruna (CZK) 1=RR 1.24. Exchange restrictions and currency controls exist relating to converting the RR into other currencies. The RR is not freely convertible in most countries outside of the Russian Federation.

#### *Accounting for the effects of inflation*

Prior to 1 January 2003 the adjustments and reclassifications made to the statutory records for the purpose of IFRS presentation included the restatement of balances and transactions for the changes in the general purchasing power of the RR in accordance with IAS 29 ("Financial Reporting in Hyperinflationary Economies"). IAS 29 requires that financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of the Russian Federation indicate that hyperinflation has ceased, effective from 1 January 2003 the Company no longer applies the provisions of IAS 29. Accordingly, the amounts expressed in the measuring unit current at 31 December 2002 are treated as the basis for the carrying amounts in these financial statements.

#### *Critical accounting estimates and judgments*

The preparation of consolidated financial statements in conformity with IFRS requires management to make prudent estimates and assumptions that affect the reported results and financial situation. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Accounting estimates will, by definition, seldom equal the actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

##### *(i) Long-term contracts*

Estimates have been made with respect to the recognition of revenue and gross margin on construction contracts including the expected "costs to complete" on such contracts. If the actual gross margins on the Group's contracts are 10% lower than management's estimates at 31 December 2004, the Group would need to reduce the carrying value of receivables recognised using the percentage-of-completion method (notes 4.14 and 22) by US\$5,154 with a corresponding effect on operating profit.

##### *(ii) Impairment*

The Group tests annually whether property, plant and equipment have suffered any impairment in accordance with accounting policy noted in note 4.7. If the estimated gross margin, which impacts the assumptions of future cash flows, at 31 December 2004 had been lower than management's estimates the Group would not need to reduce the carrying value of property, plant and equipment.

##### *(iii) Deferred taxation*

With respect to deferred taxes, management has assumed that US\$10,138 of tax losses will be utilised in the future, the effect of which is to reduce the deferred tax liability recorded at 31 December 2004 by US\$2,433. Should these tax losses not be used, the deferred tax liability would be increased by this amount with a corresponding impact on the tax charge for the year.

##### *(iv) Fair value of identifiable assets and liabilities of the acquired companies*

The management of the Company engaged the independent appraiser (American Appraisal) to appraise the fair value of identifiable assets and liabilities of the acquired ŠKODA companies (see note 6). The negative goodwill amounted to US\$113,629 and was recognised as profit. Any changes in the estimated fair values would have a corresponding effect on the amount of negative goodwill recognised in the income statement.

### 3. Basis of presentation of the financial statements (continued)

#### *Critical accounting estimates and judgments (continued)*

##### *(v) Accounting for disposal of Power Machines shares*

The Company disposed of its shares in OAO Power Machines, effectively, through an exchange of shares of OMZ, which are now classified as treasury shares. In so doing, the Company assumed that the fair value of the shares in OAO Power Machines at the time of disposal was not materially different from the purchase price it had paid approximately three months earlier after a period of extended negotiations. In making this judgement management concluded that the quoted share price of OAO Power Machines at the date of the disposal was not a reliable measure of their fair value for accounting for this transaction given that the packet of shares owned by OMZ was significantly greater than the typically traded volumes of OAO Power Machines shares. Had OMZ measured the transaction at the stock market price of OAO Power Machines shares at the date of the disposal there would have been a loss on disposal of the shares of approximately US\$ 4 million recorded in the income statement (continuing operations) and a corresponding reduction in the value of the Treasury shares balance within equity.

Other areas where judgements have been made include provisions for trade and other receivables (note 9) and provisions for inventory (note 10).

### 4. Significant accounting policies

#### 4.1 Group accounting

##### *Subsidiary undertakings*

Subsidiary undertakings, defined as those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over the operations, are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Minority interest at the balance sheet date represents the minority shareholders' portion of fair values of the identifiable assets and liabilities of the subsidiary at the acquisition date, and the minorities' portion of movements in equity since the date of the combination. Any excess of the amount paid to the minority in excess of the book value of the minority interest acquired is added to goodwill.

##### *Associated undertakings*

Associates are undertakings over which the Group generally has between 20% and 50% of the voting rights, or otherwise the Group has significant influence, but which it does not control. Investments in associated undertakings are accounted for by the equity method of accounting. The associates are initially recognised at cost and the Group's share of post-acquisition profit or loss is recognised in the income statement and its share of post-acquisition movements in reserves is recognised in its reserves. Unrealised gains on transactions between the Group and its associated undertakings are eliminated to the extent of the Group's interest; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. The Group's investment in associated undertakings includes goodwill (net of accumulated amortisation) on acquisition.

Equity accounting is discontinued when the carrying amount of the investment in an associated undertaking reaches zero, unless the Group has incurred obligations or guaranteed obligations in respect of the associated undertaking.

#### 4.2 Investments

The Group classifies its investments in the following categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale financial assets. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition and re-evaluates this designation at every reporting date.

#### 4. Significant accounting policies (continued)

##### 4.2. Investments (continued)

###### *Financial assets at fair value through profit or loss*

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorised as held for trading unless they are designated as hedges. Assets in this category are classified as current assets if they are either held for trading or are expected to be realised within 12 months of the balance sheet date.

###### *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. They are classified as current assets, except for maturities greater than 12 months after the balance sheet date, which are classified as non-current assets. Current loans and receivables are included in trade and other receivables (note 9) and non-current loans and receivables included in non-current financial assets (note 15).

###### *Available-for-sale financial assets*

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date.

Purchases and sales of investments are recognised on trade-date – the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Investments are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method. Realised and unrealised gains and losses arising from changes in the fair value of the “financial assets at fair value through profit or loss” category are included in the income statement in the period in which they arise. Unrealised gains and losses arising from changes in the fair value of non-monetary securities classified as available-for-sale are recognised in equity.

When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments are included in the income statement as gains and losses from investment securities.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models refined to reflect the issuer's specific circumstances.

##### 4.3 Cash and cash equivalents

Cash and cash equivalents consist of cash on hand and balances with banks with a maturity at the date of recognition of less than three months, which are considered by the Group at the time of deposit to have a minimal risk of default.

##### 4.4 Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less a provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the income statement.

**4. Significant accounting policies (continued)****4.5 Value added tax**

Value added tax ("VAT") related to sales is payable to the tax authorities upon the collection of receivables from customers. Input VAT is reclaimable against sales VAT upon payment for purchases. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases which have not been settled at the balance sheet date (VAT deferred) is recognised in the balance sheet on a gross basis and disclosed separately as a current asset and liability. VAT paid on advances received is presented in the balance sheet as current assets. VAT on advances received is reclaimable against the related sales VAT upon delivery of goods or services. Where provision has been made for impairment of receivables, an impairment loss is recorded for the gross amount of the debtor, including VAT. The related VAT deferred liability is maintained until the debtor is written off for tax purposes.

**4.6 Inventories**

Inventories are recorded at the lower of cost and net realisable value. The cost of inventory is determined on the first-in-first-out basis. The cost of finished goods and work in progress comprises raw material, direct labour, other direct costs and related production overhead (based on normal operating capacity) but excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

**4.7 Property, plant and equipment**

Property, plant and equipment are recorded at purchase or construction cost. At each reporting date the management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's net selling price and its value in use. The carrying amount is reduced to the recoverable amount and the difference is recognised as an expense (impairment loss) in the income statement. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

Depreciation is calculated on the restated amounts of property, plant and equipment on a straight-line basis. The depreciation periods, which approximate to the estimated useful economic lives of the respective assets, are as follows:

|                     | <u>Number of years</u> |
|---------------------|------------------------|
| Buildings           | up to 50               |
| Constructions       | up to 25               |
| Plant and machinery | up to 15               |
| Other               | up to 5                |

Land and assets under construction are not depreciated.

Repairs and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalised and the net book values of the replaced assets are written off. Gains and losses arising from the retirement of property, plant and equipment are included in the statement of income as incurred.

Interest expense on borrowings to finance the construction and purchase of property, plant and equipment is not capitalised.

**4.8 Intangible assets*****Goodwill***

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiary/associated undertaking at the date of acquisition. Goodwill on the acquisition of subsidiary undertakings is included in intangible assets. Goodwill on the acquisition of associated undertakings is included in investments in associated undertakings. Goodwill arising from business combinations for which the agreement date is before 31 March 2004 is amortised using the straight-line method over its estimated useful life. The gain or loss on disposal of an entity includes the unamortised balance of goodwill relating to the disposed entity.

**4. Significant accounting policies (continued)****4.8. Intangible assets (continued)*****Goodwill (continued)***

From the year ended 31 December 2004 onwards, goodwill is tested annually for impairment, as well as when there is an indication of impairment. Goodwill is allocated to cash-generating units for the purpose of impairment testing. The useful period for goodwill is 17 years.

The Group applies the transitional rules of IFRS 3 "Business combinations" in respect of goodwill and negative goodwill arising from business combinations for which the agreement date was before 31 March 2004. Consequently, beginning 1 January 2005, previously recognized goodwill will no longer be amortized; previously recognized negative goodwill will be derecognised, with a corresponding adjustment to the opening balance of retained earnings.

Goodwill arising from business combinations for which the agreement date is on or after 31 March 2004 is tested annually for impairment and carried at cost less accumulated impairment losses. If the cost of the acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the income statement.

***Trademarks***

Trademarks are shown at historical cost. Trademarks have a definite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of trademarks and licences over their estimated useful lives (50 years).

***Research and development***

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are recognised as an intangible asset if, and only if, it is technically feasible to complete the project, there is an intention to complete the project, it is probable that the future economic benefits that are attributable to the asset will flow to the Group and the cost of the asset can be measured reliably. Other development expenditures are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Development costs that have been capitalised are amortised from the commencement of the commercial production of the product on a straight-line basis over the period of its expected benefit. The amortisation periods adopted do not exceed ten years.

***Other intangible assets***

Expenditure on acquired patents and licences is capitalised and amortised using the straight-line method over their useful lives, which do not exceed 20 years. The useful lives of other intangible assets do not exceed 15 years.

***Impairment of other intangible assets***

Where an indication of impairment exists, the carrying amount of other intangible asset is assessed and, when impaired, the asset is written down immediately to its recoverable amount, which is the higher of net selling price and value in use.

**4.9 Negative goodwill**

Negative goodwill represents the excess of the fair value of the Group's share of the net assets acquired over the cost of acquisition.

For business combinations before 31 March 2004, to the extent that negative goodwill related to expectations of future losses and expenses that were identified in the Group's plan for the acquisition and could be measured reliably, but which did not represent identifiable liabilities, that portion of negative goodwill was recognised in the income statement when the future losses and expenses were recognised. Any remaining negative goodwill, not exceeding the fair values of the non-monetary assets acquired, was recognised in the income statement of operations over the remaining weighted average useful life of depreciable and amortisable assets acquired; negative goodwill in excess of the fair values of those assets was recognised in the income statement immediately.

The average amortisation period for negative goodwill arising from business combinations before 31 March 2004 is 11 years.



#### **4. Significant accounting policies (continued)**

##### **4.10 Borrowings**

Borrowings are recognised initially at cost, which is the fair value of the proceeds received (determined using the prevailing market rate of interest for a similar instrument, if significantly different from the transaction price), net of transaction costs incurred. In subsequent periods, borrowings are stated at amortised cost using the effective yield method; any difference between the fair value of the proceeds (net of transaction costs) and the redemption amount is recognised as interest expense over the period of the borrowings. Borrowings costs are expensed as incurred.

##### **4.11 Deferred income taxes**

Deferred tax assets and liabilities are calculated in respect of temporary differences using the balance sheet liability method for all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes. A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

##### **4.12 Provisions**

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

##### **4.13 Equity**

###### ***Share capital***

Ordinary shares and non-redeemable preferred shares with cumulative dividends are both classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction in equity from the proceeds. Any excess of the fair value of consideration received over the par value of shares issued is recognised as a share premium.

###### ***Treasury shares***

Where the Company or its subsidiaries purchase the Company's equity share capital, the consideration paid including any attributable transaction costs net of income taxes is deducted from total shareholders' equity as treasury shares until they are cancelled or reissued. Where such shares are subsequently sold or reissued, any consideration received is included in equity. Treasury shares are stated at cost.

###### ***Dividends***

Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the financial statements are authorised for issue.

#### 4. Significant accounting policies (continued)

##### 4.14 Construction contracts

Construction contracts generally include long-term contracts to manufacture design-build equipment, including nuclear power plant equipment, continuous casting machines and handling machinery.

Contract costs are recognised when incurred. When the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised only to the extent of contract costs incurred that are probable of recovery. When the outcome of a construction contract can be estimated reliably and it is probable that the contract will be profitable, contract revenue is recognised over the period of the contract. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized as an expense immediately.

The Group uses the "percentage of completion method" to determine the appropriate amount of revenues to recognise in a given period. The stage of completion is measured by reference to the contract costs incurred up to the balance sheet date as a percentage of total estimated costs for each contract.

Costs incurred in the year in connection with future activity on a contract are excluded from contract costs in determining the stage of completion. They are presented as inventories, prepayments or other assets, depending on their nature.

The Group presents as an asset the gross amount due from customers for contract work for all contracts in progress for which costs incurred plus recognised profits (less recognised losses) exceeds progress billings. Progress billings not yet paid by customers are included within trade and other receivables.

The Group presents as a liability the gross amount due to customers for contract work for all contracts in progress for which progress billings exceed costs incurred plus recognised profits (less recognised losses).

##### 4.15 Revenue recognition

Sales under contracts other than construction contracts are normally recognised when goods are shipped and the buyer accepts delivery unless these sales are conditional upon the delivery of supplementary services. In this case revenue from sales of goods and services are recognised for the contract as a whole when the services are performed; payments received for the goods are recognised until then as deferred income.

Sales are shown net of VAT and discounts, and after eliminating sales within the Group.

Sales are measured at the fair value of the consideration received or receivable. When the fair value of consideration received cannot be measured reliably, sales are measured at the fair value of the goods or services given up.

##### 4.16 Employee benefits

###### *Share-based compensation*

During 2004 the Group terminated its share option plans. Previously, the Group operated an equity-settled, share-based compensation plan with the following accounting treatment: Share options granted after November 2002 have been accounted for in accordance with provisions of IFRS 2 "Share based payments". The fair value of the employee services received in exchange for the grant of the options was recognised as an expense. The total amount to be expensed over the vesting period was determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions. Non-market vesting conditions were included in assumptions about the number of options that were expected to become exercisable. At each balance sheet date, the entity revised its estimates of the number of options that were expected to become exercisable. It recognised the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity over the remaining vesting period. The proceeds received net of any directly attributable transaction costs were credited to share capital (nominal value) and share premium when the options were exercised.

#### 4. Significant accounting policies (continued)

##### 4.16. Employee benefits (continued)

###### *Social costs*

The Group incurs employee costs related to the provision of benefits such as health services and kindergarten services. These amounts principally represent an implicit cost of employing production workers and, accordingly, have been charged to cost of sales.

###### *Pension costs*

In the normal course of business the Group contributes to the Russian Federation state pension scheme on behalf of its employees. Mandatory contributions to the governmental pension scheme are expensed when incurred. Discretionary pensions and other post-employment benefits are included in labour costs in the statement of operations; however, separate disclosures are not provided, as these costs are not material.

##### 4.17 Derivative financial instruments and hedging activities

The Group enters into financial derivative contracts solely for the purpose of hedging future cash flows. The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Amounts accumulated in equity are recycled in the income statement in the periods when the hedged item will affect profit or loss (for instance when the forecast sale that is hedged takes place). However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, inventory) or a liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

##### 4.18 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

#### 5. Segment information

##### *Primary reporting format – business segments*

The Group's continuing operations are organised into four main business segments:

*Equipment for nuclear power plants segment* (NPPEQ) production is based at Izhorskiye Zavody (Russia) and ŠKODA JS a.s. (Czech Republic) and produces three major types of equipment for the nuclear power industry:

- primary circuit equipment for nuclear power plants. A standard set of primary circuit equipment produced by the Company comprises a reactor vessel, in-vessel components, and a cover with extending pipes.
- spent nuclear fuel containers for nuclear power blocks. The Company manufactures containers for storage and transportation of spent nuclear fuel from pressurized water reactors and scientific nuclear reactors.
- a wide range of spare parts.

## 5. Segment information (continued)

### *Primary reporting format – business segments (continued)*

*Specialty steel segment* (STEEL) produces 150 specialty steel grades and a variety of castings and forgings. The Group produces high-strength structural grades, corrosion-resistant, radiation-resistant, heat-resistant, cold-resistant, non-magnetic and high-alloyed grades of steel. Standard types of casting, forging, and moulding production include retaining rings for power generating equipment, chill mould blanks, bearing ring blanks, column equipment, ship spindles, mill rolls, tank courses, as well as similar custom-made metal products. A significant part of the basic metal production is used internally as an input for machinery equipment manufacturing segment and equipment for nuclear power plants.

Specialty steels are manufactured primarily at Izhorskiye Zavody (Russia), ŠKODA HUTE s.r.o. and ŠKODA KOVARNY s.r.o. (Czech republic).

*Machinery equipment manufacturing segment* (MMEQ) produces machinery equipment based on OMZ's proprietary engineering and the production of equipment based on third party engineering, for various industries, including oil and gas, mining and metallurgical equipment.

The main production sites of the machinery equipment manufacturing segment are Uralmash and Izhorskiye Zavody (Russia).

*Mining equipment segment* (MINEQ) specializes in engineering and marketing of three major types of mining equipment: excavators (electric mining excavators and walking draglines), crushing equipment, and rock-drilling machines.

*Other business (other)*. This comprises sales of electricity and heating generated by an electricity plant located at Izhorskiye Zavody and Uralmash (Russia). It also comprises the manufacture of equipment for oil refineries and other activities.

In May 2004 the Group sold MNP comprising primarily of the oil and gas equipment and shipbuilding segments to certain members of its management (see note 7). Information, related to the results of disposed segments is presented on the face of the income statement, and assets and liabilities in the balance sheet as discontinued operations. 93% of the assets of the disposed segments were located in the Russian Federation and 51% of their sales were made in Russian Federation and Commonwealth of Independent States companies, 25% - in Europe and 24% - in Asia.

Sales or other transactions between the business segments are based on commercial terms that are available to third parties. Unallocated costs and benefits represent corporate expenses and income from the sale of non-core subsidiaries. Segment assets consist primarily of property, plant and equipment, intangible assets, inventories and receivables, and mainly exclude cash and investments. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain corporate borrowings. Capital expenditure comprises additions to property, plant and equipment, development costs and the cost of business acquisitions. Changes in provisions for impairment and other provisions relate only to those charges made against allocated assets.

## 5. Segment information (continued)

## Continuing operations

|  | 2004 | NPPEQ          | STEEL          | MMEQ            | MINEQ         | Other         | Eliminations<br>and<br>unallocated<br>items | Total<br>continuing<br>operations |
|--|------|----------------|----------------|-----------------|---------------|---------------|---|-----------------------------------|
| Total sales  |      | 145,955        | 180,518        | 160,143         | 96,306        | 105,326       | (164,451)                                   | 523,797                           |
| Less intersegment sales  |      | -              | (48,236)       | (61,187)        | -             | (55,028)      | 164,451                                     | -                                 |
| External sales   |      | 145,955        | 132,282        | 98,956          | 96,306        | 50,298        | -   | 523,797                           |
| Gross margin   |      | 33,983         | 18,181         | 19,359          | 15,866        | 16,479        | (1,854)                                     | 102,014                           |
| <b>Gross margin, %</b>   |      | <b>23%</b>     | <b>10%</b>     | <b>12%</b>      | <b>16%</b>    | <b>16%</b>    |   | <b>19%</b>                        |
| Segment result   |      | 10,084         | (2,447)        | (23,562)        | 3,321         | 1,161         | 293   | (11,150)                          |
| Unallocated operating income and expenses  |      |                |                |                 |               |               | 22,574                                      | 22,574                            |
| <b>Operating profit before negative goodwill</b>   |      | <b>10,084</b>  | <b>(2,447)</b> | <b>(23,562)</b> | <b>3,321</b>  | <b>1,161</b>  | <b>22,867</b>                               | <b>11,424</b>                     |
| Negative goodwill, recognized in profit  |      | -              | -              | -               | -             | -             | 113,907                                     | 113,907                           |
| <b>Operating profit</b>  |      | <b>10,084</b>  | <b>(2,447)</b> | <b>(23,562)</b> | <b>3,321</b>  | <b>1,161</b>  | <b>136,774</b>                              | <b>125,331</b>                    |
| Finance income/(expense)-net   |      | -              | -              | -               | -             | -             | 2,390                                       | 2,390                             |
| Loss from equity accounted investments   |      | -              | -              | -               | -             | -             | -   | -                                 |
| <b>Profit before taxation and sale of discontinued operations</b>                          |      | <b>10,084</b>  | <b>(2,447)</b> | <b>(23,562)</b> | <b>3,321</b>  | <b>1,161</b>  | <b>139,164</b>                              | <b>127,721</b>                    |
| Income tax benefit (expenses)  |      | -              | -              | -               | -             | -             | (12,724)                                    | (12,724)                          |
| <b>Profit for the year before loss from discontinued operations</b>                        |      | <b>10,084</b>  | <b>(2,447)</b> | <b>(23,562)</b> | <b>3,321</b>  | <b>1,161</b>  | <b>126,440</b>                              | <b>114,997</b>                    |
| Segment assets   |      | 414,679        | 207,080        | 115,559         | 47,257        | 37,407        | (4,978)                                     | 817,004                           |
| Unallocated assets   |      | -              | -              | -               | -             | -             | 84,040                                      | 84,040                            |
| <b>Total assets</b>  |      | <b>414,679</b> | <b>207,080</b> | <b>115,559</b>  | <b>47,257</b> | <b>37,407</b> | <b>79,062</b>                               | <b>901,044</b>                    |
| Segment liabilities  |      | 244,021        | 73,845         | 56,669          | 24,956        | 25,094        | -   | 424,585                           |
| Unallocated liabilities  |      | -              | -              | -               | -             | -             | 305,240                                     | 305,240                           |
| <b>Total liabilities</b>   |      | <b>244,021</b> | <b>73,845</b>  | <b>56,669</b>   | <b>24,956</b> | <b>25,094</b> | <b>305,240</b>                              | <b>729,825</b>                    |
| Capital expenditure  |      | 19,100         | 31,282         | 1,722           | 1,081         | 383           | -   | 53,568                            |
| Depreciation and amortisation  |      | 2,989          | 8,263          | 4,027           | 123           | 2,311         | -   | 17,713                            |
| Change in other provisions   |      | (433)          | (4,969)        | 1,691           | (909)         | (1,410)       | 955   | (5,075)                           |
| Change in provisions for impairment of property, plant and equipment and intangible assets |      | 47             | (462)          | (17,275)        | -             | (2,305)       | -   | (19,995)                          |
| Gain from release on government financing and tax penalties                                |      | -              | -              | -               | -             | -             | 9,613                                       | 9,613                             |

## 5. Segment information (continued)

## Continuing operations (continued)

|  | 2003           | NPPEQ         | STEEL          | MMEQ          | MINEQ         | Other          | Eliminations and unallocated items | Total continuing operations |
|--|----------------|---------------|----------------|---------------|---------------|----------------|------------------------------------|-----------------------------|
| Total sales  | 117,640        | 103,325       | 105,191        | 46,541        | 100,711       | (133,299)      |                                    | 340,109                     |
| Less intersegment sales  | -              | (53,798)      | (49,889)       | -             | (29,612)      | 133,299        |                                    | -                           |
| External sales   | 117,640        | 49,527        | 55,302         | 46,541        | 71,099        | -              |                                    | 340,109                     |
| Gross margin   | 47,478         | 12,051        | 15,782         | 10,892        | 16,677        | 1,914          |                                    | 104,794                     |
| <b>Gross margin, %</b>   | <b>40%</b>     | <b>12%</b>    | <b>15%</b>     | <b>23%</b>    | <b>17%</b>    |                |                                    | <b>31%</b>                  |
| Segment result   | 20,665         | 1,058         | (671)          | 2,819         | 2,305         | 1,607          |                                    | 27,783                      |
| Unallocated operating income and expenses  | -              | -             | -              | -             | -             | 4,014          |                                    | 4,014                       |
| <b>Operating profit before negative goodwill</b>   | <b>20,665</b>  | <b>1,058</b>  | <b>(671)</b>   | <b>2,819</b>  | <b>2,305</b>  | <b>5,621</b>   |                                    | <b>31,797</b>               |
| Negative goodwill, recognized in profit  |                |               |                |               |               |                |                                    | -                           |
| <b>Operating profit</b>  | <b>20,665</b>  | <b>1,058</b>  | <b>(671)</b>   | <b>2,819</b>  | <b>2,305</b>  | <b>5,621</b>   |                                    | <b>31,797</b>               |
| Finance income/(expense)-net   |                |               |                |               |               | (12,562)       |                                    | (12,562)                    |
| Loss from equity accounted investments   | (4,707)        | -             | -              | -             | -             | -              |                                    | (4,707)                     |
| <b>Profit before taxation and sale of discontinued operations</b>                          | <b>15,958</b>  | <b>1,058</b>  | <b>(671)</b>   | <b>2,819</b>  | <b>2,305</b>  | <b>(6,941)</b> |                                    | <b>14,528</b>               |
| Income tax benefit (expenses)  | -              | -             | -              | -             | -             | 1,882          |                                    | 1,882                       |
| <b>Profit for the year before loss from discontinued operations</b>                        | <b>15,958</b>  | <b>1,058</b>  | <b>(671)</b>   | <b>2,819</b>  | <b>2,305</b>  | <b>(5,059)</b> |                                    | <b>16,410</b>               |
| Segment assets   | 224,955        | 59,921        | 109,998        | 44,802        | 67,600        | (2,476)        |                                    | 504,800                     |
| Unallocated assets   | -              | -             | -              | -             | -             | 144,746        |                                    | 144,746                     |
| <b>Total assets</b>  | <b>224,955</b> | <b>59,921</b> | <b>109,998</b> | <b>44,802</b> | <b>67,600</b> | <b>142,270</b> |                                    | <b>649,546</b>              |
| Segment liabilities  | 124,882        | 25,065        | 38,722         | 12,006        | 29,410        | -              |                                    | 230,085                     |
| Unallocated liabilities  | -              | -             | -              | -             | -             | 300,365        |                                    | 300,365                     |
| <b>Total liabilities</b>   | <b>124,882</b> | <b>25,065</b> | <b>38,722</b>  | <b>12,006</b> | <b>29,410</b> | <b>300,365</b> |                                    | <b>530,450</b>              |
| Capital expenditure  | 3,610          | 802           | 14,632         | 112           | 6,989         | -              |                                    | 26,145                      |
| Depreciation and amortisation  | 1,987          | 1,572         | 1,756          | -             | 2,461         | -              |                                    | 7,776                       |
| Change in other provisions   | (34)           | (2,708)       | 144            | 109           | (86)          | -              |                                    | (2,575)                     |
| Change in provisions for impairment of property, plant and equipment and intangible assets | -              | -             | 7,365          | -             | (2,925)       | -              |                                    | 4,440                       |
| Gain from release on government financing and tax penalties                                | -              | -             | -              | -             | -             | 2,738          |                                    | 2,738                       |

## Secondary reporting format – geographical segments

## Continuing operations

The Group's four business segments operate in five main geographical areas:

|                                    | Sales          |                | Total assets   |                | Capital expenditure |               |
|------------------------------------|----------------|----------------|----------------|----------------|---------------------|---------------|
|                                    | 2004           | 2003           | 2004           | 2003           | 2004                | 2003          |
| Russian Federation                 | 252,010        | 203,805        | 554,266        | 645,910        | 9,531               | 20,611        |
| Commonwealth of Independent States | 31,665         | 9,691          | 4,211          | -              | -                   | -             |
| Asia                               | 157,414        | 108,721        | -              | -              | -                   | -             |
| Europe                             | 81,203         | 14,227         | 342,567        | -              | 44,029              | -             |
| Other regions                      | 1,505          | 3,665          | -              | 3,636          | 8                   | 5,534         |
| <b>Total</b>                       | <b>523,797</b> | <b>340,109</b> | <b>901,044</b> | <b>649,546</b> | <b>53,568</b>       | <b>26,145</b> |

Sales are based on the geographical area in which the customer is located. Assets and capital expenditure are based on the geographical area where the assets are located.

## 6. Business combinations

Business combinations were accounted for as an acquisition in accordance with IFRS 3 "Business Combinations". The identifiable assets and liabilities of acquired subsidiaries were recognised at the fair value of the identifiable assets and liabilities acquired as at the date of acquisition and minority interest recognised at the minority shareholders' portion of fair values of the identifiable assets and liabilities of the subsidiary at the acquisition date.

### Acquisitions in 2004

In July 2004 the Group acquired a 100 percent share in three companies (ŠKODA JS a.s. and ŠKODA STEEL (which includes ŠKODA HUTE s.r.o. and ŠKODA KOVARNY s.r.o.)) from ŠKODA HOLDING a.s. a member of Appian group controlled by Appian Central European Development Investment Fund(s) Plc Limited and Appian Group PLC.

ŠKODA, KOVÁRNÝ, Plzeň, s.r.o. is a limited liability company registered in the Register of Companies maintained by the Regional Court in Plzeň, the Czech Republic, registration date 1 April 1993. The main activities of the Company are forging and metal machining.

ŠKODA, HUTĚ, Plzeň, s. r. o. is a limited liability company registered in the Register of Companies maintained by the Regional Court in Plzeň, the Czech Republic, registration date 5 March 1993. The main activities of the Company are casting of ferrous and non-ferrous metals, metal machining, pattern manufacturing and cabinet making.

ŠKODA JS a.s. is primarily engaged in manufacturing nuclear and chemical facilities, as well as facilities for other industries, such as heavy welding, construction activities, the operation, maintenance, repair, modernisation and disposal of nuclear and non-nuclear energy facilities, and facilities related to the chemical and petrochemical industry.

The acquired business contributed revenues of US\$90,138 and a net loss of US\$4,019 to the Group for the period from 1 July 2004 to 31 December 2004. If the acquisition had occurred on 1 January 2004, the acquired companies' contributes to revenues would have been US\$192,927, and the net loss would have been US\$11,586.

The impact of acquisitions of subsidiaries on the consolidated financial statements was as follows:

|  | ŠKODA companies  |                           |
|--|------------------|---------------------------|
|  | Fair value       | Acquiree's carrying value |
| Percentage of share capital acquired         | 100              | 100                       |
| Cash and cash equivalents                    | 23,581           | 23,581                    |
| Accounts receivable and prepayments          | 47,576           | 47,576                    |
| Inventories                                  | 29,280           | 28,873                    |
| Other current assets                         | 375              | 375                       |
| Property, plant and equipment                | 84,780           | 63,928                    |
| Intangible assets                            | 34,428           | 393                       |
| Long-term bank deposits                      | 20,526           | 20,526                    |
| Other non-current assets                     | 37,589           | 37,589                    |
| Trade and other payables                     | (76,397)         | (76,397)                  |
| Deferred tax asset (liability)               | (9,787)          | 996                       |
| Other long-term liabilities                  | (36,172)         | (36,172)                  |
| <b>Net assets at acquisition date</b>        | <b>155,779</b>   | <b>111,268</b>            |
| Minority interest                            | -                | -                         |
| <b>Net assets acquired</b>                   | <b>155,779</b>   | <b>111,268</b>            |
| Consideration                                | 42,150           |                           |
| <b>Negative goodwill</b>                     | <b>(113,629)</b> |                           |
| Cash paid by the Company during 2004         | 17,762           |                           |
| Less cash of acquired subsidiary             | (23,581)         |                           |
| <b>Cash flow on acquisition, net of cash</b> | <b>(5,819)</b>   |                           |

**6. Business combinations (continued)****Acquisitions in 2004 (continued)**

Details of the purchase price for the ŠKODA acquisition were as follows:

|                                       |               |
|---------------------------------------|---------------|
| – Deposits made in 2003               | 5,041         |
| – Cash paid during 2004               | 17,762        |
| – Amount outstanding, payable in 2005 | 20,822        |
| Exchange difference                   | (1,475)       |
| <b>Total purchase consideration</b>   | <b>42,150</b> |

The negative goodwill, which is the excess fair value of identifiable net assets and liabilities over purchase consideration is attributable to the fact that the previous shareholder of ŠKODA companies accepted a price of US\$ 42 million in order to effect a rapid disposal of their interests to a single buyer.

**Other acquisitions**

During 2004 the Group increased its share in OMZ Sibir by 25% for US\$1,078. At 31 December 2004 this amount was still payable. This acquisition gave rise to negative goodwill of US\$278.

Negative goodwill in the amount of US\$113,907 was written off to income statement at the date of acquisition in accordance with IFRS 3 (revised 2004) "Business combinations".

**Acquisitions in 2003**

The impact of acquisitions of subsidiaries on the consolidated financial statements in 2003 was as follows:

|   | CKB Korall   | Volgograd<br>shipbuilding<br>plant | Zarubezh<br>energoproekt | Biolink<br>Technologies<br>International<br>Inc. |
|---|--------------|------------------------------------|--------------------------|--|
| Percentage of share capital acquired                  | 94.3         | 71.0                               | 50.9                     | 38.6   |
| Cash and cash equivalents                             | 1,452        | 2,488                              | 52                       | 85   |
| Accounts receivable and prepayments                   | 440          | 3,602                              | 126                      | 189  |
| Inventories   | 441          | 4,185                              | 176                      | 851  |
| Other current assets                                  | 28           | 3,428                              | 23                       | 418  |
| Property, plant and equipment                         | 2,446        | 12,782                             | 923                      | 120  |
| Intangible assets                                     | 70           | -                                  | 114                      | -  |
| Other non-current assets                              | 2            | 996                                | 20                       | -  |
| Trade and other payables                              | (495)        | (11,196)                           | (430)                    | (773)  |
| Long-term borrowings                                  | -            | -                                  | -                        | (41)   |
| Long-term taxes payable                               | (11)         | -                                  | -                        | -  |
| Deferred tax liability                                | (507)        | (189)                              | -                        | -  |
| <b>Net assets at acquisition date</b>                 | <b>3,866</b> | <b>16,096</b>                      | <b>1,004</b>             | <b>849</b>                                       |
| Minority interest                                     | 220          | 4,665                              | 493                      | 521  |
| <b>Net assets acquired</b>                            | <b>3,646</b> | <b>11,431</b>                      | <b>511</b>               | <b>328</b>                                       |
| Consideration   | 4,665        | 6,811                              | 1,204                    | 5,738  |
| <b>Goodwill (negative goodwill)</b>                   | <b>1,019</b> | <b>(4,620)</b>                     | <b>693</b>               | <b>5,410</b>                                     |
| Cash paid by the Company                              | 2,534        | 6,637                              | 1,158                    | 3,482  |
| Less cash of acquired subsidiary                      | (1,452)      | (2,488)                            | (52)                     | (85)   |
| <b>Cash flow on acquisition, net of cash acquired</b> | <b>1,082</b> | <b>4,149</b>                       | <b>1,106</b>             | <b>3,397</b>                                     |
| <b>Profit (loss) for the year</b>                     | <b>380</b>   | <b>(314)</b>                       | <b>30</b>                | <b>(3,944)</b>                                   |

Volgograd shipbuilding plant is a shipyard specializing in the building of civil ships located in Volgograd, Russia acquired in July 2003. This was disposed in 2004 as part of the sale of MNP to the management (see note 7).

CKB Korall is a research and development institute specializing in the design and engineering of offshore oil drilling and production units, located in Sevastopol, Ukraine, acquired in October 2003. This was disposed in 2004 as part of



**6. Business combinations (continued)****Acquisitions in 2003 (continued)**

Zarubezhenergoproekt is a research and development institute specializing in engineering and new technology development for both nuclear and traditional energy generation plants, located in Ivanovo, Russia, acquired in April 2003.

BioLink is a security technology provider specializing in the development, manufacturing and marketing of advanced fingerprint biometric products, located in Florida, USA. The Group achieved effective control over Biolink in June 2003 through a majority of voting shares totalling 51 percent.

In 2003 the Group also settled a payable totalling US\$6,895 in respect of the acquisition of Almaz, which took place in 2002.

During 2003 the Group increased its share in the following subsidiaries:

|                   | Consideration paid | Additional share, % |
|-------------------|--------------------|---------------------|
| Uralmash          | 3,729              | 5.0%                |
| Izhorskiye Zavody | 2,777              | 4.7%                |
| Other             | 234                |                     |
|                   | <b>6,740</b>       |                     |

During 2003 OMZ exchanged 41 thousand ordinary shares in treasury for 8 thousand additional ordinary shares of Uralmash and 204 thousand ordinary shares held in treasury for 23 thousand additional ordinary shares of Izhorskiye Zavody (subsidiaries of the Company). As a result of these transactions the Company's share in Uralmash increased by 0.2 percent and share in Izhorskiye Zavody increased by 1.3 percent. The acquisition of additional shares in subsidiaries was accounted for at the market price of the Company's shares at the date of the transactions. In addition to these exchanges of shares, the total cash consideration on the acquisition of additional shares was US\$4,525 representing 4.8% of the additional shares in Uralmash and 3.4% of the remaining shares in Izhorskiye Zavody.

**7. Balances and transactions with related parties**

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24 (revised 2003) "Related Party Disclosures".

During 2004 and 2003, the Company had transactions or balances with the following companies which were under the significant influence of management or shareholders:

| Name of related party                      | Type of relationship                                    |
|--|---|
| ОАО Atomenergoexport (AEE)                 | Associate (see below)                                   |
| ЗАО Atomstroyexport (ASE)                  | Subsidiary of AEE (see below)                           |
| ООО Invest Aktiv                           | Subsidiary of AEE (see below)                           |
| ОАО Power Machines                         | Significant influence by OMZ key management (see below) |
| BioLink Technologies International         | Significant influence by OMZ shareholders               |
| Promtorgbank                               | Significant influence by OMZ shareholders               |
| ОАО Industrial Group NIPEK-Bioprocess      | Significant influence by OMZ shareholders               |
| ЗАО Neftyanoi Investitsionnyi Dom          | Significant influence by OMZ shareholders               |
| ООО NitsTyazhMash                          | Significant influence by OMZ shareholders               |
| ООО Machinery Engineering Russia           | Significant influence by OMZ shareholders               |
| ООО Industrial Investments holding company | Significant influence by OMZ shareholders               |

On 20 September 2004 the Group sold its investment in ОАО Atomenergoexport (AEE) and since this date AEE and

**7. Balances and transactions with related parties (continued)**

In 2002, the Company entered into a long-term agreement related to the construction of the Kudan-Kulam nuclear power plant in India. These long-term agreements were conducted with Atomstroyexport ("ASE"), which acts as general contractor for all construction projects at nuclear power plants conducted by the Russian Federation in foreign countries.

During the first nine months of 2004 sales to ASE totalled US\$67,547 (US\$98,512 in 2003 for continuing operations and for entity), which amounted to approximately 13 % of total sales of the Group for 2004 (approximately 18% in 2003). At 31 December 2003, the amount due from ASE of US\$50,318 represents trade receivables for dispatched nuclear power plant equipment.

In February 2004 a merger with OAO Power Machines was initially agreed and in March 2004 OMZ acquired 11 percent of the ordinary shares of OAO Power Machines for US\$42,500. In April 2004 Mr. Yakovlev (Chief Executive Officer of OAO Power Machines) was appointed as the Company's Chief Executive Officer as a result of the proposed transaction with OAO Power Machines.

On June 30, 2004 OMZ sold the shares of OAO Power Machines, following the reversal of the previous merger agreement, by effectively exchanging them for OMZ shares (this swap was accounted for at cost and recorded as a reduction in equity arising from the purchase of treasury shares). See comments in note 3 Basis of presentation of the financial statements within critical accounting estimates and judgements (v) regarding the loss which would have been recognised on the transaction had different assumptions been applied. On 16 August 2004 Mr. Yakovlev ceased to be the Chief Executive Officer of the Company, and since that date OAO Power Machines is no longer a related party to the Group. During the first seven months of 2004 sales to OAO Power Machines totalled US\$7,509.

Accounts receivable from related parties consisted of the following:

|  | Continuing operations |                | Entity         |
|--|-----------------------|----------------|----------------|
|  | 2004                  | 2003           | 2003           |
| ZAO Atomstroyexport  | -                     | 50,318         | 50,318         |
| ZAO Atomstroyexport - due from customers for contract work           | -                     | 48,570         | 48,570         |
| OOO Invest Aktiv   | -                     | 11,270         | 11,270         |
| OOO Industrial Investments Holding Company                           | 238                   | -              | -              |
| OOO Resource   | 119                   | 112            | 112            |
| Promtorgbank   | 6,844                 | 5,562          | 5,652          |
| Other  | -                     | 32             | 137            |
|  | <b>7,201</b>          | <b>115,864</b> | <b>116,059</b> |
| Classified as accounts due from customers for contract work (note 9) | -                     | (48,570)       | (48,570)       |
|  | <b>7,201</b>          | <b>67,294</b>  | <b>67,489</b>  |

At 31 December 2004 accounts receivable from Promtorgbank mainly consisted of promissory notes issued by Promtorgbank (at 31 December 2003 – bank deposits in Promtorgbank).

At 31 December 2003 accounts receivable from OOO Invest Aktiv represented an interest-free loan in the amount of US\$11,270. This was received during 2004.

On 20 May 2004 the Group sold to certain members of the management (Nikolaev S.V., Zharkov N.S, Lipsky S.V., Grabovec L.G., Aivasov M.G., Andriyashin V.P., Kosolapov M.V.) the oil and gas equipment and shipbuilding business segments. Although Lipsky S.V. and Nikolaev S.V continue to work in OMZ, in total they held less than 20% of MNP shares at 20 May 2004 and their shares were sold by the end of the year and they did not have any influence on MNP's transactions, therefore the transactions with MNP were not considered as related party transactions after the date of disposal (May 2004).

The share of OMZ Group in the net assets of MNP at the date of disposal was US\$103,975 for consideration received of US\$50,000. In addition, at the date of disposal MNP companies had borrowings totalling US\$71,657, including a VTB loan of US\$44,964.

**7. Balances and transactions with related parties (continued)**

Accounts receivable from related parties, long-term, consisted of the following:

|  | Continuing operations |      | Entity |
|--|-----------------------|------|--------|
|  | 2004                  | 2003 | 2003   |
| Promtorgbank                               | -                     | 948  | 948    |
| Other                                      | -                     | -    | 1,753  |
| Total due from related parties – long-term | -                     | 948  | 2,701  |

Accounts payable to related parties consisted of the following:

|   | Continuing operations |                | Entity         |
|---|-----------------------|----------------|----------------|
|   | 2004                  | 2003           | 2003           |
| ZAO Atomstroyexport   | -                     | 92,682         | 95,111         |
| OOO Industrial Investments Holding Company                  | 213                   | -              | -              |
| Promtorgbank  | 13                    | 10,470         | 13,643         |
| Other   | 405                   | 175            | 916            |
|   | <b>631</b>            | <b>103,327</b> | <b>109,670</b> |
| Classified as advances received for contract work (note 17) | -                     | (92,682)       | (92,682)       |
|   | <b>631</b>            | <b>10,645</b>  | <b>16,988</b>  |

At 31 December 2003 the weighted average effective interest rate on RR denominated and US dollar loans from Promtorgbank totalled 15.4 percent and 11.4 percent, respectively for continuing operations and 15.4 percent and 11.3 percent for entity.

The interest expense included in the consolidated income statement on loans from Promtorgbank amounted to US\$382 in 2004, and US\$722 in 2003 for continuing operations and US\$747 for entity.

Cash held in the Promtorgbank bank account at 31 December 2004 totalled US\$3,066 ( 31 December 2003: US\$4,277 for continuing operations and US\$6,742 for entity).

The fair value of these balances approximates their carrying amounts.

**Key management compensation**

The remuneration paid to the directors of the Company is determined in respect of the period from one annual general meeting to the next. The most recent annual general meetings of the Company were held on 16 November 2004 and on 30 June 2003. During the years ended 31 December 2004 and 2003, the aggregate compensation to the directors included in general and administrative expenses in the consolidated income statement amounted to US\$2,879 and US\$2,925, respectively.

In addition, each director who was a member of the board of directors as at 28 June 2001 had an option to purchase up to 1 thousand shares for US\$3.66 per share as part of the remuneration approved at the annual general meeting of the Company on 28 June 2001 and each of the directors who was a member of the board of directors as at 26 June 2002 had an option to purchase up to 10 thousand shares for US\$5.17 per share which was approved at the annual general meeting of the Company on 26 June 2002. All of the share options approved in 2001 were exercised in March 2003 whilst the share options approved in 2002 were exercised in December 2003. In December 2002 three members of the board of directors, Mr. Bendookidze, Mr. Kazbekov and Mr. Kosolapov, received share options of 42 thousand, 42 thousand and 40 thousand shares, respectively, each at US\$0.1 per share as compensation for services during the years 2000-2002. These share options were exercised in February 2003 and were recognised in the Group's consolidated income statement for the year ended 31 December 2002 at a cost of US\$707.

In addition to the share options referred to above, in December 2002 the board of directors of the Company approved two share option plans for its top executives. These share option programs were terminated during 2004 (note 21).

**7. Balances and transactions with related parties (continued)****Key management compensation (continued)**

Share option type "A" was approved for the Company's top executives, to become effective on 1 January 2003. Under this share option plan 97.5 thousand of the Company's common treasury shares were vested over a one year period as compensation for the executives' services during 2003. The exercise price of the share option was US\$0.5 per share. The value of top executives' services in respect of this share option scheme was recognised in the Group's consolidated income statement for the year ended 31 December 2003 at a cost of US\$563.

Under the Share option type "B", 266 thousand of the Company's common treasury shares could vest over the period from 2003 to 2005, and 520 thousand shares could vest over the period from 2003 to 2006. The exercise price of these share options was US\$0.5 per share. The full vesting of 266 thousand shares was conditional upon the Company's share price reaching US\$11 over the three year period ending 31 December 2005, and the vesting of 520 thousand shares was conditional on the share price reaching \$11.5 during the four years ending 31 December 2006. Among other conditions, share option agreements with executives for 730 thousand shares specified that the options vested upon a change of the Chief Executive Officer.

The cost of these two share option schemes was recognised in the Group's consolidated income statement for the year ended 31 December 2003 at a cost of US\$3,999. During 2004 no other share options programs were approved and no cost was therefore recorded.

As at 31 December 2003, the Company had provided guarantees in respect of certain members of senior management of up to US\$187. As at 31 December 2004, there were no guarantees remaining.

**8. Cash and cash equivalents**

Cash and cash equivalents comprise the following:

|  | Continuing operations |              | Entity        |
|--|-----------------------|--------------|---------------|
|  | 2004                  | 2003         | 2003          |
| RR denominated cash on hand and balances with banks  | 5,153                 | 6,780        | 12,883        |
| CZK denominated cash on hand and balances with banks | 12,756                | -            | -             |
| EURO denominated balances with banks                 | 5,464                 | 212          | 1,274         |
| US\$ denominated balances with banks                 | 936                   | 677          | 7,106         |
| Other currency denominated balances with bank        | 84                    | 380          | 2,798         |
|  | <b>24,393</b>         | <b>8,049</b> | <b>24,061</b> |

**9. Trade and other receivables**

|   | Continuing operations |                | Entity         |
|---|-----------------------|----------------|----------------|
|   | 2004                  | 2003           | 2003           |
| Trade receivables                                     | 140,689               | 33,567         | 31,257         |
| Receivable from related parties (note 7)              | 7,201                 | 67,294         | 67,489         |
| Accounts due from customers for contract work         | 80,087                | 61,727         | 77,201         |
| VAT recoverable                                       | 43,163                | 34,991         | 51,031         |
| VAT on advances from customers                        | 21,670                | 18,652         | 21,124         |
| Other taxes receivable                                | 7,750                 | 9,500          | 13,040         |
| Advances to suppliers                                 | 103,869               | 33,663         | 84,598         |
| Forward foreign exchange contracts – cash flow hedges | 3,475                 | -              | -              |
| Other receivables                                     | 35,332                | 22,474         | 10,398         |
|   | <b>443,236</b>        | <b>281,868</b> | <b>356,138</b> |

Accounts receivable are denominated in Russian Roubles except for US\$214,592 and US\$54,732 of accounts receivable denominated in US dollars and CZK at 31 December 2004 respectively (at 31 December 2003 US\$49,031 and nil CZK for continuing operations; US\$58,401 and nil CZK for entity)

**9. Trade and other receivables (continued)**

Provisions for impairment offset against the account receivable balances are as follows:

|                       | Continuing operations |                | Entity         |
|-----------------------|-----------------------|----------------|----------------|
|                       | 2004                  | 2003           | 2003           |
| Trade receivables     | (6,094)               | (6,191)        | (7,468)        |
| Taxes receivable      | -                     | -              | (173)          |
| Advances to suppliers | (2,518)               | (655)          | (729)          |
| Other receivables     | (6,684)               | (1,276)        | (1,457)        |
|                       | <b>(15,296)</b>       | <b>(8,122)</b> | <b>(9,827)</b> |

The fair value of net accounts receivable approximate their carrying amounts.

**10. Inventories**

|                                  | Continuing operations |                | Entity         |
|----------------------------------|-----------------------|----------------|----------------|
|                                  | 2004                  | 2003           | 2003           |
| Raw materials                    | 60,108                | 58,272         | 91,921         |
| Work in progress                 | 82,636                | 68,393         | 88,980         |
| Finished goods                   | 40,381                | 35,356         | 50,052         |
| Goods in transit                 | 802                   | 5,956          | 5,958          |
| Provision for obsolete inventory | (38,632)              | (35,195)       | (42,288)       |
|                                  | <b>145,295</b>        | <b>132,782</b> | <b>194,623</b> |

Certain inventories included above totalling US\$41,505 (2003: US\$73,409 for continuing operations and US\$74,059 for Entity) were provided as security under loan agreements (note 18). At 31 December 2004 inventories totalling US\$5,719 were carried at fair value less costs to sell (31 December 2003: US\$1,948 related to continuing operations and US\$1,948 for Entity).

The cost of write-down of inventories recognised as expense amounted to US\$3,770 in 2004 (2003: US\$2,756 for continuing and US\$4,136 for Entity).

**11. Other current financial assets**

|  | Continuing operations |              | Entity       |
|--|-----------------------|--------------|--------------|
|  | 2004                  | 2003         | 2003         |
| Financial assets at fair value through profit and loss | 3,512                 | 3,366        | 4,374        |
| Deposits with banks                                    | -                     | 1,414        | 3,879        |
|  | <b>3,512</b>          | <b>4,780</b> | <b>8,253</b> |

At 31 December 2004 financial assets at fair value through profit and loss represent mainly RR denominated bank promissory notes with a weighted average interest rate of 14 percent (31 December 2003: 14 percent for continuing operations and 10 percent for Entity) which management intends to sell within 12 months from the balance sheet date. At 31 December 2003 financial assets at fair value through profit and loss for continuing operations also includes promissory notes, issued by subsidiaries disposed in 2004, of US\$2 912 (see Note 3).

The weighted average interest rate on deposits with banks at 31 December 2003 amounted to 10% percent for US\$1,414 of RR denominated deposits for continuing operations. (1.6 percent of US\$1,815 US dollar denominated deposits and 8.8 percent of US\$2,064 of RR denominated deposits for Entity).

## 12. Property, plant and equipment

|   | Land and<br>buildings | Machinery and<br>equipment | Other        | Assets under<br>construction | Total          |
|---|-----------------------|----------------------------|--------------|------------------------------|----------------|
| <b>Balance at 31 December 2003</b>                      |                       |                            |              |                              |                |
| <b>Discontinued operations</b>                          |                       |                            |              |                              |                |
| Cost  | 73,190                | 29,494                     | 5,892        | 3,642                        | 112,218        |
| Accumulated depreciation                                | (13,511)              | (15,606)                   | (2,519)      | -                            | (31,636)       |
| Impairment loss recognised                              | -                     | (149)                      | (78)         | -                            | (227)          |
| <b>Net book value discontinued operations</b>           | <b>59,679</b>         | <b>13,739</b>              | <b>3,295</b> | <b>3,642</b>                 | <b>80,355</b>  |
| <b>Continuing operations</b>                            |                       |                            |              |                              |                |
| Cost  | 149,804               | 169,864                    | 17,158       | 12,393                       | 349,219        |
| Accumulated depreciation                                | (70,598)              | (112,965)                  | (10,050)     | -                            | (193,613)      |
| Impairment loss recognised                              | (12)                  | (10,781)                   | (753)        | (10,491)                     | (22,037)       |
| <b>Net book value continuing operations</b>             | <b>79,194</b>         | <b>46,118</b>              | <b>6,355</b> | <b>1,902</b>                 | <b>133,569</b> |
| <b>Net book value of the entity at 31 December 2003</b> | <b>138,873</b>        | <b>59,857</b>              | <b>9,650</b> | <b>5,544</b>                 | <b>213,924</b> |
| Disposal of discontinued operations                     | (68,796)              | (15,630)                   | (3,449)      | (3,643)                      | (91,518)       |
| Exchange differences                                    | 9,980                 | 7,828                      | 395          | 420                          | 18,623         |
| Disposal of non-core businesses units (note 26)         | -                     | (40)                       | (170)        | (100)                        | (310)          |
| Addition through acquisition of subsidiaries (note 6)   | 41,351                | 43,303                     | 2,125        | 1,343                        | 88,122         |
| Additions   | 1,447                 | 7,999                      | 383          | 228                          | 10,057         |
| Disposals   | (4,480)               | (2,578)                    | (1,925)      | (108)                        | (9,091)        |
| Depreciation  | (4,341)               | (10,294)                   | (2,239)      | -                            | (16,874)       |
| Impairment (charge) release                             | 1,895                 | (13,325)                   | (778)        | 573                          | (11,635)       |
| <b>Closing net book value</b>                           | <b>115,929</b>        | <b>77,120</b>              | <b>3,992</b> | <b>4,257</b>                 | <b>201,298</b> |
| <b>Balance at 31 December 2004</b>                      |                       |                            |              |                              |                |
| Cost  | 182,136               | 231,150                    | 23,260       | 13,043                       | 449,589        |
| Accumulated depreciation                                | (63,612)              | (133,188)                  | (17,176)     | -                            | (213,976)      |
| Impairment loss recognised                              | (2,595)               | (20,842)                   | (2,092)      | (8,786)                      | (34,315)       |
| <b>Net book value at 31 December 2004</b>               | <b>115,929</b>        | <b>77,120</b>              | <b>3,992</b> | <b>4,257</b>                 | <b>201,298</b> |

Comparative information for the year 2003:

|   | Land and<br>buildings | Machinery and<br>equipment | Other        | Assets under<br>construction | Total          |
|---|-----------------------|----------------------------|--------------|------------------------------|----------------|
| <b>Balance at 31 December 2002</b>                    |                       |                            |              |                              |                |
| Cost  | 210,026               | 190,688                    | 21,922       | 23,385                       | 446,021        |
| Accumulated depreciation                              | (89,388)              | (129,027)                  | (11,595)     | -                            | (230,010)      |
| Impairment loss recognised                            | (12)                  | (17,558)                   | (1,737)      | (12,201)                     | (31,508)       |
| <b>Net book value</b>                                 | <b>120,626</b>        | <b>44,103</b>              | <b>8,590</b> | <b>11,184</b>                | <b>184,503</b> |
| Opening net book value                                | 120,626               | 44,103                     | 8,590        | 11,184                       | 184,503        |
| Exchange differences                                  | 9,151                 | 3,277                      | 540          | 821                          | 13,789         |
| Addition through acquisition of subsidiaries (note 6) | 12,566                | 2,798                      | 882          | 25                           | 16,271         |
| Additions   | 5,478                 | 14,669                     | 2,906        | (6,566)                      | 16,487         |
| Disposals   | (713)                 | (2,113)                    | (535)        | (1,630)                      | (4,991)        |
| Depreciation  | (8,235)               | (7,864)                    | (2,988)      | -                            | (19,087)       |
| Impairment release                                    | -                     | 4,987                      | 255          | 1,710                        | 6,952          |
| <b>Closing net book value</b>                         | <b>138,873</b>        | <b>59,857</b>              | <b>9,650</b> | <b>5,544</b>                 | <b>213,924</b> |
| <b>Balance at 31 December 2003</b>                    |                       |                            |              |                              |                |
| Cost  | 222,994               | 199,358                    | 23,050       | 16,035                       | 461,437        |
| Accumulated depreciation                              | (84,109)              | (128,571)                  | (12,569)     | -                            | (225,249)      |
| Impairment loss recognised                            | (12)                  | (10,930)                   | (831)        | (10,491)                     | (22,264)       |
| <b>Net book value at 31 December 2003</b>             | <b>138,873</b>        | <b>59,857</b>              | <b>9,650</b> | <b>5,544</b>                 | <b>213,924</b> |

**12. Property, plant and equipment (continued)**

In 2004 the fixed assets of the acquired ŠKODA companies were appraised by an independent appraiser and were accounted for at fair value.

At 31 December 2004 bank borrowings are secured on properties with a carrying value of US\$13,650 (2003: US\$18,029- continuing operations and US\$18,922 for Entity) (Note 18).

At 31 December 2004 and 31 December 2003 the gross carrying value of fully depreciated property, plant and equipment was US\$113,521 and US\$93,475 respectively for continuing operations and US\$99,362 at 31 December 2003 for Entity.

In the year ended 31 December 2004, management assessed the recoverable amount of property, plant and equipment and the adequacy of impairment losses and release recognised in prior periods. An impairment charge totalling US\$13,112 was recorded in 2004 in relation to Uralmash property, plant and equipment, which relates to the machinery equipment manufacturing segment, mainly due to a significant increase of raw materials prices and a corresponding reassessment of the future cash flows. In 2003 there was a release of US\$6,394, mainly due to a decrease in the discount rate applied to future cash flows. Discount rates of 10.9 percent and 16.0 percent for US dollar denominated and Russian Rouble denominated cash flows, respectively, have been used in estimating the recoverable value through discounted cash flows at 31 December 2004 (12.2 percent and 19.6 percent at 31 December 2003).

Land and buildings include 120 plots of land in Bolevec (Czech Republic) with a total area of 336,511 square meters and 36 plots in Plzen (Czech Republic) with a total area of 126,523 square meters. Uralmash and Izhorskiye Zavody signed 20-49 year rental agreements, under which rent payments are negotiated annually.

**13. Deposit on investments**

Deposit on investments at 31 December 2003 represented balances on escrow accounts for the acquisition of ŠKODA companies. The deposit balance was applied in partial settlement of the purchase price of the transaction during 2004.

**14. Intangible assets**

|  | Goodwill      | Trade marks   | Other         | Total         |
|--|---------------|---------------|---------------|---------------|
| <b>Balance at 31 December 2003</b>                       |               |               |               |               |
| <b>Discontinued operations</b>                           |               |               |               |               |
| Cost   | 8,574         | -             | 14,405        | 22,979        |
| Accumulated amortisation                                 | -             | -             | (14)          | (14)          |
| Impairment loss recognised                               | (4,633)       | -             | (13,923)      | (18,556)      |
| Net book value discontinued operations                   | <b>3,941</b>  | <b>-</b>      | <b>468</b>    | <b>4,409</b>  |
| <b>Continuing operations</b>                             |               |               |               |               |
| Cost   | 7,035         | -             | 3,592         | 10,627        |
| Accumulated amortisation                                 | (200)         | -             | (622)         | (822)         |
| Impairment loss recognised                               | -             | -             | -             | -             |
| Net book value continuing operations                     | <b>6,835</b>  | <b>-</b>      | <b>2,970</b>  | <b>9,805</b>  |
| <b>Net book value of the entity at 31 December 2003</b>  | <b>10,776</b> | <b>-</b>      | <b>3,438</b>  | <b>14,214</b> |
| Disposal of discontinued operations                      | (3,773)       | -             | (1,362)       | (5,135)       |
| Additions through acquisition of subsidiaries (note 6)   | -             | 15,119        | 23,688        | 38,807        |
| Additions  | -             | -             | 283           | 283           |
| Disposal of non-core businesses (note 26)                | (2,306)       | -             | (93)          | (2,399)       |
| Amortisation (for goodwill acquired before 1 April 2004) | (380)         | (152)         | (1,599)       | (2,131)       |
| Impairment charge  | (3,818)       | -             | -             | (3,818)       |
| Exchange differences                                     | 256           | 691           | 1,183         | 2,130         |
| Closing net book value                                   | <b>755</b>    | <b>15,658</b> | <b>25,538</b> | <b>41,951</b> |
| <b>Balance at 31 December 2004</b>                       |               |               |               |               |
| Cost   | 5,152         | 15,816        | 27,853        | 48,821        |
| Accumulated amortisation                                 | (579)         | (158)         | (2,315)       | (3,052)       |
|  | (2,818)       |               |               | (2,818)       |

**14. Intangible assets (continued)**

Comparative information for the year 2003:

|   | Goodwill      | Other        | Total         |
|---|---------------|--------------|---------------|
| <b>Balance at 31 December 2002</b>  |               |              |               |
| Cost  | 5,693         | 14,489       | 20,182        |
| Accumulated amortisation  | (37)          | (560)        | (597)         |
| Impairment loss recognised  | (2,813)       | (12,904)     | (15,717)      |
| Net book value  | <b>2,843</b>  | <b>1,025</b> | <b>3,868</b>  |
| Addition through acquisition of subsidiary                                | 7,122         | 252          | 7,374         |
| Addition through acquisition of additional share in subsidiaries (note 6) | 3,808         | -            | 3,808         |
| Additions   | -             | 2,346        | 2,346         |
| Disposals   | -             | (40)         | (40)          |
| Amortisation  | (163)         | (226)        | (389)         |
| Impairment charge   | (2,839)       | -            | (2,839)       |
| Exchange differences  | 5             | 81           | 86            |
| Closing net book value  | <b>10,776</b> | <b>3,438</b> | <b>14,214</b> |
| <b>Balance at 31 December 2003</b>  |               |              |               |
| Cost  | 15,609        | 17,997       | 33,606        |
| Accumulated amortisation  | (200)         | (636)        | (836)         |
| Impairment loss recognised  | (4,633)       | (13,923)     | (18,556)      |
| Net book value at 31 December 2003  | <b>10,776</b> | <b>3,438</b> | <b>14,214</b> |

Trade marks consist of trade marks "ŠKODA" used by ŠKODA JS a.s. and ŠKODA Kovarny s.r.o. The fair values of these trade marks were evaluated by American Appraisal using the income approach, referred to as the "relief from royalty" method.

Other intangible assets mostly consist of patented and non-patented technologies (net book value at 31 December 2004 is US\$13,781 and US\$0 at 31 December 2003) and research and development costs (net book value at 31 December 2004 is US\$4,973 and US\$896 at 31 December 2003).

**15. Non-current financial assets**

|   | Continuing operations |              | Entity        |
|---|-----------------------|--------------|---------------|
|   | 2004                  | 2003         | 2003          |
| Receivable from Vneshtorgbank ("VTB")                 | -                     | -            | 36,806        |
| Available for-sale financial assets                   | 5,465                 | 3,208        | 3,688         |
| Receivable from related parties (note 7)              | -                     | 948          | 2,701         |
| Advances issued                                       | 16,168                | 586          | 632           |
| Forward foreign exchange contracts – cash flow hedges | 715                   | -            | -             |
| Accounts due from customers for contract work         | 10,798                | -            | -             |
| Long-term bank deposits                               | 21,633                | -            | -             |
| Other receivables                                     | 1,888                 | 2,248        | 6,024         |
|   | <b>56,667</b>         | <b>6,990</b> | <b>49,851</b> |

As at 31 December 2004 long-term advances issued represent mainly advances paid by ŠKODA JS a.s. for long-term contracts.

Accounts due from customers for contract work represent the amount receivable under the agreements related to the construction of the Liang Yung Gang nuclear power plant in China.

At 31 December 2004 available for-sale financial assets are mainly represented by investments in Promtorgbank (PTB) of US\$1,661 (2.73% of PTB share capital), in OAO Power Machines of US\$1,285 (0.37% of its shares) and in UJV Rez of US\$2,042 (17.4% of the shares) (31 December 2003: investments in PTB shares of US\$1,824, and in ZAO Transkat of US\$460, sold in 2004).



**15. Non-current financial assets (continued)**

As at 31 December 2003, the Company owed Vneshtorgbank US\$36.8 million in connection with an order received by the Group for a diesel submarine for the Chinese Navy through Rosoboronexport. Pursuant to an arrangement with Vneshtorgbank, Vneshtorgbank issued a guarantee to the Chinese Ministry of Defence in respect of Rosoboronexport's performance bond, which was issued as a result of advance payments made to the Group through Rosoboronexport. Due to a statutory requirement that significant bank guarantees are collateralised, the Company provided Vneshtorgbank with promissory notes issued by Vneshtorgbank and purchased by the Group with funds advanced to the Company by Vneshtorgbank by way of an unsecured loan of US\$36.8 million. Both the promissory notes and the unsecured loan denominated in US dollars, bear effective interest at a rate of 8.4 percent and mature in September 2005. These assets and liabilities were effectively disposed of as part of the sale of discontinued operations. The VTB promissory notes were classified in the balance sheet as other non-current assets and the loan payable to VTB was classified as other non-current liabilities at 31 December 2003 (note 20).

An amount of US\$21,633 deposited in bank accounts is assigned specifically to guarantee contractual agreements with customers and will be released gradually as the individual projects are completed.

**16. Negative goodwill**

|  |                 |
|--|-----------------|
| <b>Balance at 31 December 2003</b>                     |                 |
| Discontinued operations                                | (15,519)        |
| Continuing operations                                  | (26,977)        |
| <b>Balance of the Entity at 31 December 2003</b>       | <b>(42,496)</b> |
| Disposal of discontinued operations                    | 17,879          |
| Disposal related to sold property, plant and equipment | 2,373           |
| Amortisation   | 1,292           |
| Exchange differences                                   | (1,427)         |
| <b>Balance at 31 December 2004</b>                     | <b>(22,379)</b> |

Comparative information for the year 2003:

|  |                 |
|--|-----------------|
|  | <b>2003</b>     |
| <b>Balance at 31 December 2002</b>   | <b>(33,709)</b> |
| Acquisition of additional shares in subsidiaries and additions through acquisitions of subsidiaries (note 6) | (9,222)         |
| Amortisation   | 3,102           |
| Exchange differences   | (2,667)         |
| <b>Balance at 31 December 2003</b>   | <b>(42,496)</b> |

**17. Trade and other accounts payable**

|   | <b>Continuing operations</b> |                | <b>Entity</b>  |
|---|------------------------------|----------------|----------------|
|   | <b>2004</b>                  | <b>2003</b>    | <b>2003</b>    |
| Trade payables  | 107,898                      | 32,699         | 36,352         |
| Payables to related parties (note 7)                    | 631                          | 10,645         | 16,988         |
| Advances received                                       | 49,946                       | 38,527         | 63,405         |
| Advances received for contract work                     | 125,885                      | 92,682         | 92,682         |
| Accounts due to customers for contract work             | 49,194                       | -              | 17,779         |
| Deferred VAT  | 30,373                       | 21,788         | 22,772         |
| Short-term portion of long-term taxes payable (note 19) | 5,746                        | 5,648          | 6,255          |
| Other taxes payable                                     | 10,242                       | 15,884         | 25,317         |
| Payroll accounts payable                                | 9,584                        | 8,718          | 14,555         |
| Provisions for liabilities and charges (note 29)        | 18,384                       | 5,792          | 15,026         |
| Other payables and accrued expenses                     | 54,009                       | 21,763         | 12,365         |
|   | <b>461,892</b>               | <b>254,146</b> | <b>323,496</b> |

At 31 December 2004 accounts payable were primarily denominated in Russian Roubles except for US\$163,985 and US\$106,209 of accounts payable denominated in US dollars and Czech Koruna respectively. (at 31 December 2003 US\$95 911 for continuing operations and US\$96 456 for Entity both denominated in US dollars)

**18. Borrowings****Short-term borrowings**

|   | Continuing operations |                | Entity         |
|---|-----------------------|----------------|----------------|
|   | 2004                  | 2003           | 2003           |
| Banks:  |                       |                |                |
| US\$ denominated fixed rate                   | 61,746                | 48,763         | 49,074         |
| RR denominated fixed rate                     | 47,149                | 80,788         | 91,185         |
| US\$ denominated floating rate                | 9,116                 | 30,182         | 30,182         |
| EURO denominated floating rate                | 688                   | 648            | 648            |
| Romanian lei fixed rate                       | -                     | -              | 590            |
|   | <b>118,699</b>        | <b>160,381</b> | <b>171,679</b> |
| Other US\$ denominated fixed rate             | -                     | 2,500          | 3,501          |
| Other RR denominated fixed rate               | -                     | 4,537          | 2,589          |
|   | <b>118,699</b>        | <b>167,418</b> | <b>177,769</b> |
| Add: current portion of non-convertible bonds | -                     | 26,482         | 26,482         |
| Add: current portion of long-term debt        | 3,346                 | 1,136          | 1,136          |
|   | <b>122,045</b>        | <b>195,036</b> | <b>205,387</b> |

At 31 December 2004 other RR denominated fixed rate short-term borrowings include borrowings from MNP companies in the amount of US\$2,003.

The effective interest rates at the balance sheet dates were as follows:

|                                   | Continuing operations |                | Entity           |
|-----------------------------------|-----------------------|----------------|------------------|
|                                   | 2004                  | 2003           | 2003             |
| Banks:                            |                       |                |                  |
| US\$ denominated fixed rate       | 8.79%                 | 6.96%          | 10.20%           |
| RR denominated fixed rate         | 10.31%                | 8.15%          | 11.00%           |
| US\$ denominated floating rate    | 6.41%                 | LIBOR plus 4.2 | LIBOR plus 4.2   |
|                                   | EURIBOR plus          | EURIBOR plus   | EURIBOR plus 4.2 |
| EURO denominated floating rate    | 5.5                   | 4.2            |                  |
| Romanian lei fixed rate           |                       |                | 23.00%           |
| Other US\$ denominated fixed rate | -                     | 3.20%          | 3.20%            |
| Other RR denominated fixed rate   | -                     | 4.10%          | 4.10%            |

As at 31 December 2004, short-term borrowings totalling US\$13,650 and US\$38,394 ( 31 December 2003: US\$55,105 and US\$30,023) are secured on the property and inventory of the Group, respectively for continuing operations. The Group total amounts of borrowings secured on the property and inventory at 31 December 2003 were US\$55,998 and US\$30,023. The carrying amount of pledged inventory and property, plant and equipment is disclosed in notes 10 and 12, respectively.

**Long-term borrowings**

|   | Continuing operations |               | Entity        |
|---|-----------------------|---------------|---------------|
|   | 2004                  | 2003          | 2003          |
| Banks:  |                       |               |               |
| RR denominated fixed rate                       | 37,124                | 10,864        | 10,864        |
| US\$ denominated fixed rate                     | 37,100                | -             | -             |
| US\$ denominated floating rate                  | 1,664                 | 2,839         | 2,839         |
| EURO denominated floating rate                  | 621                   | 380           | 380           |
| Romanian lei fixed rate                         | -                     | -             | 183           |
|   | <b>76,509</b>         | <b>14,083</b> | <b>14,266</b> |
| Non-convertible bonds                           | 24,275                | 57,038        | 57,038        |
|   | <b>100,784</b>        | <b>71,121</b> | <b>71,304</b> |
| Less : current portion of non-convertible bonds | -                     | (26,482)      | (26,482)      |
| Less: current portion of long-term debt         | (3,346)               | (1,136)       | (1,136)       |
| Total long-term borrowings                      | <b>97,438</b>         | <b>43,503</b> | <b>43,686</b> |

**18. Borrowings (continued)****Long-term borrowings (continued)**

The effective interest rates at the balance sheet dates were as follows:

|                                | Continuing operations |                  | Entity           |
|--------------------------------|-----------------------|------------------|------------------|
|                                | 2004                  | 2003             | 2003             |
| Banks:                         |                       |                  |                  |
| RR denominated fixed rate      | 10.94%                | 10.50%           | 10.50%           |
| US\$ denominated floating rate | 9.21%                 | -                | -                |
| EURO denominated floating rate | LIBOR plus 6.35       | LIBOR plus 6.4   | LIBOR plus 6.4   |
| Romanian lei fixed rate        | EURIBOR plus 4.2      | EURIBOR plus 4.2 | EURIBOR plus 4.2 |
| US\$ denominated fixed rate    |                       |                  | 24.00%           |
| Non-convertible bonds          | 13.49%                | 14.40%           | 14.40%           |

The re-pricing period for Floating interest rates is every six months.

At 31 December 2004 long-term loans had the following maturity profile:

|                                | 2005         | 2006          | 2007          | 2008 and after | Total          |
|--------------------------------|--------------|---------------|---------------|----------------|----------------|
| Banks:                         |              |               |               |                |                |
| US\$ denominated floating rate | 832          | 832           | -             | -              | 1,664          |
| EURO denominated floating rate | 414          | 207           | -             | -              | 621            |
| US\$ denominated fixed rate    | 2,100        | -             | 35,000        | -              | 37,100         |
| RR denominated fixed rate      | -            | 32,376        | 4,748         | -              | 37,124         |
|                                | <b>3,346</b> | <b>33,415</b> | <b>39,748</b> | -              | <b>76,509</b>  |
| Non-convertible bonds          | -            | -             | -             | 24,275         | 24,275         |
|                                | <b>3,346</b> | <b>33,415</b> | <b>39,748</b> | <b>24,275</b>  | <b>100,784</b> |

The Group is required to make an offer for early repayment of non-convertible bonds at par totalling US\$24,275 in September 2005.

At 31 December 2003 long-term loans related to continuing operations had the following maturity profile:

|                                | 2004          | 2005          | 2006         | 2007 and after | Total         |
|--------------------------------|---------------|---------------|--------------|----------------|---------------|
| Banks:                         |               |               |              |                |               |
| RR denominated fixed rate      | -             | 10,864        | -            | -              | 10,864        |
| US\$ denominated floating rate | 756           | -             | 2,083        | -              | 2,839         |
| EURO denominated floating rate | 380           | -             | -            | -              | 380           |
|                                | <b>1,136</b>  | <b>10,864</b> | <b>2,083</b> | -              | <b>14,083</b> |
| Non-convertible bonds          | 26,482        | -             | -            | 30,556         | 57,038        |
|                                | <b>27,618</b> | <b>10,864</b> | <b>2,083</b> | <b>30,556</b>  | <b>71,121</b> |

At 31 December 2003 long-term loans for Entity had the following maturity profile:

|                                | 2004          | 2005          | 2006         | 2007 and after | Total         |
|--------------------------------|---------------|---------------|--------------|----------------|---------------|
| Banks:                         |               |               |              |                |               |
| RR denominated fixed rate      | -             | 10,864        | -            | -              | 10,864        |
| US\$ denominated floating rate | 756           | -             | 2,083        | -              | 2,839         |
| EURO denominated floating rate | 380           | -             | -            | -              | 380           |
| Romanian lei fixed rate        | -             | -             | 183          | -              | 183           |
|                                | <b>1,136</b>  | <b>10,864</b> | <b>2,266</b> | -              | <b>14,266</b> |
| Non-convertible bonds          | 26,482        | -             | -            | 30,556         | 57,038        |
|                                | <b>27,618</b> | <b>10,864</b> | <b>2,266</b> | <b>30,556</b>  | <b>71,204</b> |

**18. Borrowings (continued)****Long-term borrowings (continued)**

The carrying amounts and fair values of long-term debt are as follows:

|                       | Continuing operations |             |                  |             | Entity           |                    |
|-----------------------|-----------------------|-------------|------------------|-------------|------------------|--------------------|
|                       | 2004                  |             | 2003             |             | 2003             |                    |
|                       | Carrying amounts      | Fair values | Carrying amounts | Fair values | Carrying amounts | Fair value amounts |
| Banks                 | 73,163                | 73,163      | 12,947           | 12,522      | 13,130           | 12,705             |
| Non-convertible bonds | 24,275                | 24,275      | 30,556           | 30,852      | 30,556           | 30,852             |

The fair value of long-term debt is estimated by discounting the future contractual cash outflows at the market interest rate available to the Group at the balance sheet date of 9.5 percent for US\$ denominated borrowings and 11.5 percent for RR denominated borrowings (31 December 2003: 10 percent for US dollar denominated and 15 percent for RR denominated for continuing operations and Entity).

As at 31 December 2004, long-term borrowings totalling nil and US\$3,111 (31 December 2003: US\$1,513 and US\$10,866) included above are secured on the property, plant and equipment and inventory of the Group, respectively. The carrying amount of pledged inventory and property, plant and equipment is disclosed in notes 10 and 12, respectively. Furthermore, at 31 December 2004, long-term borrowing in the amount of US\$32,434 is secured on 31.5% of the ordinary shares of OAO Izhorskiye Zavody.

At 31 December 2004, the Group short-term borrowings from ING Bank in amount of US\$35,000 was secured by the guarantee of VTB.

At 31 December 2004 the Group had unused borrowing facilities of US\$107,975 (31 December 2003: US\$21,950 for continuing operations and US\$21,950 for Entity).

**Domestic non-convertible bonds**

|  |               |
|--|---------------|
| <b>Balance at 1 January 2003</b>                         | <b>28,599</b> |
| Issuance (par value RR 1 thousand totalling RR'mln 900)  | 30,556        |
| Repayment (par value RR 1 thousand totalling RR'mln 130) | (4,389)       |
| Amortization of discount                                 | 14            |
| Exchange differences                                     | 2,258         |
| <b>Balance at 31 December 2003</b>                       | <b>57,038</b> |
| Repayment (par value RR 1 thousand totalling RR'mln 780) | (27,359)      |
| Repayment (par value RR 1 thousand totalling RR'mln 226) | (7,740)       |
| Effect of exchange rate changes                          | 2,336         |
| <b>Balance at 31 December 2004</b>                       | <b>24,275</b> |

**19. Long-term taxes payable**

Long-term taxes payable mainly comprise various taxes payable to the state and local budgets and non-budget funds of the Russian Federation which were previously past due and which have been restructured to be repaid over a period of up to 10 years.

|  | Continuing operations |               | Entity        |
|--|-----------------------|---------------|---------------|
|  | 2004                  | 2003          | 2003          |
| Current  | 5,746                 | 5,648         | 6,255         |
| 1 to 2 years                                     | 7,945                 | 5,291         | 6,472         |
| 2 to 3 years                                     | 314                   | 9,843         | 10,538        |
| 3 to 4 years                                     | 88                    | 3,251         | 3,436         |
| 4 to 5 years                                     | 70                    | 3,038         | 3,232         |
| Thereafter                                       | 1,589                 | 5,159         | 5,489         |
| Total restructured                               | <b>15,752</b>         | <b>32,230</b> | <b>35,422</b> |
| Less: current portion of taxes payable (note 17) | (5,746)               | (5,648)       | (6,255)       |
| Long-term portion of restructured taxes          | <b>10,006</b>         | <b>26,582</b> | <b>29,167</b> |

**19. Long-term taxes payable (continued)**

At 31 December 2004 long-term taxes payable bore an effective interest rate of 5.5 percent per annum (31 December 2003: 5.5 percent).

The fair value of long-term taxes payable at 31 December 2004 totalled US\$8,805 (31 December 2003: US\$19,489- for continuing operations and US\$23,752 – for entity). The fair value of long-term taxes payable is estimated by discounting the future cash outflows in accordance with the terms of restructured tax agreements at the market interest rate available to the Group at the balance sheet date of 11.5 percent (31 December 2003: 15 percent).

**20. Other long-term liabilities**

|                             | Continuing operations |              | Entity        |
|-----------------------------|-----------------------|--------------|---------------|
|                             | 2004                  | 2003         | 2003          |
| Payable to VTB (note 15)    | -                     | -            | 36,806        |
| Other long-term liabilities | 8,877                 | 1,905        | 2,709         |
|                             | <b>8,877</b>          | <b>1,905</b> | <b>39,515</b> |

At 31 December 2004 other long-term liabilities comprised letters of credit, related to an agreement with Syrian Petroleum Company, for the supply of electrical drilling rigs. The amount of US\$5,080 is payable in 2006 and US\$3,797 in 2007.

**21. Equity**

|  | Number of outstanding shares (thousands) |                 | Number of treasury shares (thousands) |                 | Share capital     |                 | Treasury shares   |                 |
|--|--|-----------------|---------------------------------------|-----------------|-------------------|-----------------|-------------------|-----------------|
|  | Preference shares                        | Ordinary shares | Preference shares                     | Ordinary shares | Preference shares | Ordinary shares | Preference shares | Ordinary shares |
| <b>At 1 January 2002</b>                         | <b>2,750</b>                             | <b>35,350</b>   | -                                     | (3,975)         | <b>26</b>         | <b>340</b>      | -                 | (38)            |
| Currency translation                             | -  | -               | -                                     | -               | 2                 | 26              | -                 | -               |
| Employees share option scheme:                   |  |                 |                                       |                 |                   |                 |                   |                 |
| - proceeds from sale of treasury shares          | -  | -               | -                                     | 510             | -                 | -               | -                 | 2               |
| Acquisition of additional shares in subsidiaries | -  | -               | -                                     | 245             | -                 | -               | -                 | 3               |
| <b>At 31 December 2003</b>                       | <b>2,750</b>                             | <b>35,350</b>   | -                                     | (3,220)         | <b>28</b>         | <b>366</b>      | -                 | (33)            |
| Currency translation                             | -  | -               | -                                     | -               | 2                 | 23              | (1,183)           | (896)           |
| Additional issue of shares                       | -  | 130             | -                                     | -               | -                 | -               | -                 | -               |
| Employees share option scheme:                   |  |                 |                                       |                 |                   |                 |                   |                 |
| - proceeds from sale of treasury shares          | -  | -               | -                                     | 730             | -                 | -               | -                 | 105             |
| Purchase of treasury shares                      | -  | -               | (2,720)                               | (2,061)         | -                 | -               | (24,179)          | (18,321)        |
| <b>At 31 December 2004</b>                       | <b>2,750</b>                             | <b>35,480</b>   | <b>(2,720)</b>                        | <b>(4,551)</b>  | <b>30</b>         | <b>389</b>      | <b>(25,362)</b>   | <b>(19,145)</b> |

At 31 December 2004 the authorised number of ordinary and preference shares totalled 70,700 thousand and 2,750 thousand (31 December 2003: 35,350 thousand and 2,750 thousand), respectively, both with a nominal value per share of RR 0.1.

At 31 December 2004 the issued number of ordinary and preference shares totalled 35,480 thousand and 2,750 thousand. (31 December 2003: 35,350 thousand and 2,750 thousand).

Preference shares represent cumulative preferred stock without voting rights, except in certain circumstances pertaining to the liquidation or reorganization of the Company, or changes in the charter documents. They earn dividends at 12% per annum of their nominal value, and have a liquidation value of RR 0.1 per share.

Treasury shares represent ordinary and preference shares owned by subsidiaries. In accordance with the Company's corporate governance policy these shares represent non-voting stock.

**21. Equity (continued)**

During 2004 the Group exchanged treasury ordinary shares for preference shares at a ratio of four ordinary shares for five preference shares. Accordingly, 2,176 thousand treasury ordinary shares were exchanged for 2,720 thousand preference shares.

At 31 December 2004 the hedging reserve represented the effective portion of changes in the fair value of derivatives in the amount of US\$812.

A dividend was declared in 2004 in respect of 2003 to holders of preference shares of RR 0.012 per share (in 2003 in respect of 2002 RR 0.012 per share). No dividend was declared on ordinary shares during 2004 and 2003.

The statutory accounting reports of the Company are the basis for profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the net profit. For 2004, the current year net statutory profit for the Company as reported in the published annual statutory reporting forms was equivalent to US\$160. However, this legislation and other statutory laws and regulations dealing with distribution rights are open to legal interpretation and accordingly management believes at present it would not be appropriate to disclose an amount as "distributable reserves" in these financial statements.

**Share options**

In December 2002, the Company's Board of Directors approved a plan to distribute 442.5 thousand treasury shares to the Company's employees at a price of US\$0.1 per share as compensation for their services during the period 2000-2002. 124 thousand of these share options were granted to the Company's key management (note 7). These share options were recognised in the Group's consolidated income statement for the year ended 31 December 2002 at a cost of US\$2,490.

Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

|                        | 2004                               |                                 | 2003                               |                                 |
|------------------------|------------------------------------|---------------------------------|------------------------------------|---------------------------------|
|                        | Average<br>exercise<br>price, US\$ | Share<br>options<br>(thousands) | Average<br>exercise<br>price, US\$ | Share<br>options<br>(thousands) |
| Balance at 1 January   | 0.5                                | 893                             | 0.6                                | 1,164                           |
| Granted                | -                                  | -                               | 0.5                                | 239                             |
| Exercised              | 0.5                                | (730)                           | 0.8                                | (510)                           |
| Expired                | 0.6                                | (163)                           | -                                  | -                               |
| Balance at 31 December | -                                  | -                               | -                                  | 893                             |

In 2004 the share option program was terminated (note 7).

The fair value of options granted during 2003, determined using the Black-Scholes valuation model, was US\$3,999. The significant inputs into the model were share price of US\$5.825, at the grant date, exercise price discussed above (note 7), standard deviation of expected share price returns of 32%, option life (note 7), and annual risk-free interest rate of 3.10%. The volatility measured at the standard deviation of the expected share price returns is based on a statistical analysis of weekly share prices over the last three years.

During 2004 the weighted average market price of the Company's shares was US\$7.7 (2003: US\$6.4).

**22. Construction contracts**

During 2004 the revenues and gross margin recognised on long-term-contracts amounted to:

|                  | Continuing operations |          | Entity    |
|------------------|-----------------------|----------|-----------|
|                  | 2004                  | 2003     | 2003      |
| Contract revenue | 95,869                | 98,018   | 215,470   |
| Contract costs   | (78,166)              | (64,983) | (163,053) |
| Gross margin     | 17,703                | 33,035   | 52,417    |

**22. Construction contracts (continued)**

The Group's financial position with respect to construction contracts is disclosed in notes 9 and 17.

Construction contracts in progress:

|  | Continuing operations |         |
|--|-----------------------|---------|
|  | 2004                  | 2003    |
| Contract costs incurred and recognised profits (less losses) to date | 1,045,069             | 184,040 |
| Advances received on construction contracts                          | 211,223               | 95,852  |

At 31 December 2004 the contract costs incurred and recognised profits (less losses) to date in the amount of US\$790,774 and the advances received on construction contracts in the amount of US\$86,611 related to ŠKODA JS a.s.

**23. Cost of sales**

|   | Continuing operations |                | Entity         |
|---|-----------------------|----------------|----------------|
|   | 2004                  | 2003           | 2003           |
| Changes in inventories of finished goods and work in progress | (25,373)              | (7,921)        | (17,188)       |
| Materials and components used                                 | 246,292               | 102,436        | 177,767        |
| Labor costs   | 71,956                | 67,853         | 115,161        |
| Gas and fuel  | 53,218                | 38,301         | 65,846         |
| Services  | 40,400                | 19,191         | 9,919          |
| Depreciation  | 14,537                | 7,424          | 17,370         |
| Amortisation of intangible assets                             | 1,040                 | -              | -              |
| Amortisation of negative goodwill                             | (1,292)               | (1,131)        | (3,102)        |
| Other   | 21,005                | 9,162          | 27,206         |
|   | <b>421,783</b>        | <b>235,315</b> | <b>392,979</b> |

**24. Selling expenses**

|                | Continuing operations |               | Entity        |
|----------------|-----------------------|---------------|---------------|
|                | 2004                  | 2003          | 2003          |
| Transportation | 6,563                 | 3,255         | 3,869         |
| Services       | 11,037                | 6,899         | 8,833         |
| Labour costs   | 2,658                 | 736           | 906           |
| Other          | 900                   | 1,303         | 1,367         |
|                | <b>21,158</b>         | <b>12,193</b> | <b>14,975</b> |

**25. General and administrative expenses**

|                             | Continuing operations |               | Entity         |
|-----------------------------|-----------------------|---------------|----------------|
|                             | 2004                  | 2003          | 2003           |
| Taxes                       | 6,736                 | 9,407         | 12,344         |
| Labour costs                | 45,247                | 41,618        | 59,012         |
| Amortisation of intangibles | 1,091                 | -             | 389            |
| Depreciation                | 2,337                 | 1,483         | 1,717          |
| Services                    | 20,081                | 26,533        | 28,316         |
| Administration overheads    | 7,591                 | 6,721         | 14,647         |
|                             | <b>83,083</b>         | <b>85,762</b> | <b>116,425</b> |

## 26. Other operating income and expenses

|  | Continuing operations |               | Entity        |
|--|-----------------------|---------------|---------------|
|  | 2004                  | 2003          | 2003          |
| Profit from sales of non-core subsidiaries                             | 21,352                | 14,666        | 14,666        |
| Change in provision for impairment of receivables (note 9)             | (889)                 | (1,158)       | (2,245)       |
| Change in provision for obsolete inventory (note 10)                   | (4,186)               | (1,417)       | (5,618)       |
| Impairment release (charge) on property, plant and equipment (note 12) | (13,871)              | 7,279         | 6,952         |
| Impairment charge on intangible assets (note 14)                       | (6,124)               | (2,839)       | (2,839)       |
| Gain (loss) on disposal of property, plant and equipment               | 6,831                 | 3,149         | 2,940         |
| Gain on release from government financing and tax penalties            | 9,613                 | 2,738         | 3,094         |
| Other  | 925                   | 2,540         | 1,591         |
|  | <b>13,651</b>         | <b>24,958</b> | <b>18,541</b> |

During 2004, the management of the Company disposed of the following non-core subsidiaries:

|                       | Consideration | Profit from sales of non-core subsidiaries |
|-----------------------|---------------|--|
| OOO GTEK              | 10,005        | 5,937                                      |
| OOO ZSMK              | 4,500         | 5,307                                      |
| OOO Izhora-Energosbit | 8,097         | 4,082                                      |
| OOO Instrument        | 7,081         | 4,378                                      |
| Other                 | 3,043         | 1,648                                      |
|                       | <b>32,726</b> | <b>21,352</b>                              |

In 2004 the cash received from the sale of these non-core subsidiaries amounted to US\$12,553. At 31 December 2004 the amount receivable is US\$20,173.

During 2003, the management of the Company disposed of its metallurgical equipment business to Severstalmash. Under the agreement Severstalmash acquired the sales and marketing organization and engineering expertise of the metallurgical equipment business as well as the right to use the corresponding trademarks for a total consideration of US\$14 million. The sale resulted in the recognition of a gain of US\$13 million. The disposal did not result in the transfer of any of the Company's production facilities to Severstalmash.

## 27. Finance income/(expense) -net

|   | Continuing operations |                 | Entity         |
|---|-----------------------|-----------------|----------------|
|   | 2004                  | 2003            | 2003           |
| Interest expense on borrowings  | (26,583)              | (20,535)        | (21,205)       |
| Interest expense on restructured taxes payable  | (526)                 | (623)           | (1,070)        |
| Interest income   | 2,477                 | 1,041           | 2,002          |
| Gain (loss) on financial assets through profit and loss and available-for-sale financial assets | 5,255                 | (773)           | (1,072)        |
| Foreign exchange gain   | 21,767                | 8,328           | 12,837         |
|   | <b>2,390</b>          | <b>(12,562)</b> | <b>(8,508)</b> |

## 28. Income tax

|   | Continuing operations |              | Entity         |
|---|-----------------------|--------------|----------------|
|   | 2004                  | 2003         | 2003           |
| Income tax expense/(credit) – current   | (1,082)               | (613)        | (4,061)        |
| Deferred tax expense/(income) – origination and reversal of temporary differences | (11,642)              | 2,495        | (177)          |
| <b>Income tax (benefit) expense</b>   | <b>(12,724)</b>       | <b>1,882</b> | <b>(4,238)</b> |



**28. Income tax(continued)**

The income before taxation for financial reporting purposes is reconciled to the tax expense as follows:

|   | Continuing operations |                | Entity       |
|---|-----------------------|----------------|--------------|
|   | 2004                  | 2003           | 2003         |
| <b>Profit before taxation and sale of discontinued operations</b>                 | 127,721               | 14,528         | 26,926       |
| Theoretical tax charge at statutory rate of 24% (2003 – 24%)                      | 30,653                | 3,487          | 6,462        |
| Tax effect of items which are not deductible or assessable for taxation purposes: |                       |                |              |
| Tax penalties and release of government financing                                 | (2,307)               | (2,211)        | (544)        |
| Write-off of negative goodwill  | (27,338)              | -              | -            |
| Impairment of goodwill  | 1,470                 | -              | -            |
| Loss from disposal on non-core businesses   | 6,881                 | -              | -            |
| Write-off of bad debts  | 1,303                 | -              | -            |
| Other non-deductible expenses   | 2,752                 | 2,469          | 3,755        |
| Non-recognised deferred tax asset movement  | (690)                 | (5,627)        | (5,435)      |
| <b>Income tax (benefit) expense</b>   | <b>12,724</b>         | <b>(1,882)</b> | <b>4,238</b> |

Most companies in the Group were subject to tax rates of 24 percent on taxable profits for the year 2004 and 2003 (except ŠKODA companies –28% in 2003-2004, 26% in 2005, 24% in 2006). Deferred tax asset and liabilities are mainly measured at the rate of 24 percent as at 31 December 2004 (31 December 2003: 24 percent).

|  | 31<br>December<br>2003 | Addition<br>through<br>acquisition of<br>subsidiaries | Disposal of<br>subsidiaries | Exchange<br>difference | Differences<br>recognition<br>and reversals | 31<br>December<br>2004 |
|--|------------------------|---|-----------------------------|------------------------|---|------------------------|
| <b>Tax effects of deductible temporary differences:</b>                    |                        |   |                             |                        |   |                        |
| Provision for impairment of property, plant and equipment                  | 10,057                 | 2,950   | (3,972)                     | 464                    | 665   | 10,164                 |
| Provision for impairment of receivables                                    | 2,624                  | 731   | (425)                       | 130                    | (3,060)                                     | -                      |
| Provision for impairment of investments                                    | 2,648                  | -   | (1,789)                     | 88                     | (162)                                       | 785                    |
| Accounts payable and accruals  | 2,021                  | 2,898   | (1,569)                     | 87                     | 176   | 3,613                  |
| Provision for inventory  | 11,107                 | 1,246   | (1,696)                     | 567                    | (1,022)                                     | 10,202                 |
| Accounts receivable  | 5,947                  | 1,018   | (114)                       | 355                    | 110   | 7,316                  |
| Loss carry-forward   | 1,964                  | 4,666   | (1,964)                     | 131                    | (1,195)                                     | 3,602                  |
| Other  | 2,997                  | -   | (1,922)                     | 82                     | (757)                                       | 400                    |
| <b>Tax effects of taxable temporary differences:</b>                       |                        |   |                             |                        |   |                        |
| Hyperinflation and fair value adjustments on property, plant and equipment | (13,386)               | (15,488)  | 10,014                      | (589)                  | 580   | (18,869)               |
| Production overheads recognized for tax purposes                           | (14,372)               | -   | 4,248                       | (305)                  | (119)                                       | (10,548)               |
| Accounts receivable recognized using percentage-of-completion method       | (12,671)               | -   | 6,529                       | (620)                  | (2,364)                                     | (9,126)                |
| Provision for impairment of receivables                                    | -                      | -   | -                           | (238)                  | (3,370)                                     | (3,608)                |
| Other  | (3,785)                | (1,705)   | 918                         | (260)                  | (1,814)                                     | (6,646)                |
| <b>Net tax effect of temporary differences</b>                             | <b>(4,849)</b>         | <b>(3,684)</b>  | <b>8,258</b>                | <b>(108)</b>           | <b>(12,332)</b>                             | <b>(12,715)</b>        |
| Less non-recognised deferred tax asset                                     | (6,330)                | (6,139)   | 3,011                       | (572)                  | 690   | (9,340)                |
| <b>Total net deferred tax (liability)/assets</b>                           | <b>(11,179)</b>        | <b>(9,823)</b>  | <b>11,269</b>               | <b>(680)</b>           | <b>(11,642)</b>                             | <b>(22,055)</b>        |

## 28. Income tax(continued)

Comparative information for the year 2003:

|  | 31<br>December<br>2002 | Addition through<br>acquisition of<br>subsidiaries | Exchange<br>difference | Differences<br>recognition and<br>reversals | 31<br>December<br>2003 |
|--|------------------------|--|------------------------|---|------------------------|
| <b>Tax effects of deductible temporary differences:</b>                    |                        |  |                        |   |                        |
| Provision for impairment on property, plant and equipment                  | 11,820                 | -  | 741                    | (2,504)                                     | 10,057                 |
| Provision for impairment of receivables                                    | 2,376                  | -  | 190                    | 58  | 2,624                  |
| Provision for impairment of investments                                    | 1,692                  | -  | 166                    | 790   | 2,648                  |
| Accounts payable and accruals  | 3,292                  | -  | 198                    | (1,469)                                     | 2,021                  |
| Provision for inventories  | 8,815                  | 284  | 751                    | 1,257                                       | 11,107                 |
| Accounts receivable  | 2,936                  | 48   | 343                    | 2,620                                       | 5,947                  |
| Loss carry-forward   | 748                    | -  | 105                    | 1,111                                       | 1,964                  |
| Other  | 2,797                  | 567  | 219                    | (586)                                       | 2,997                  |
| <b>Tax effects of taxable temporary differences:</b>                       |                        |  |                        |   |                        |
| Hyperinflation and fair value adjustments on property, plant and equipment | (11,397)               | (1,595)  | (863)                  | 469   | (13,386)               |
| Production overheads recognized for tax purposes                           | (12,596)               | -  | (1,046)                | (730)                                       | (14,372)               |
| Accounts receivable recognized using percentage-of-completion method       | (7,320)                | -  | (771)                  | (4,580)                                     | (12,671)               |
| Other  | (1,541)                | -  | (196)                  | (2,048)                                     | (3,785)                |
| <b>Net tax effect of temporary differences</b>                             | <b>1,622</b>           | <b>(696)</b>                                       | <b>(163)</b>           | <b>(5,612)</b>                              | <b>(4,849)</b>         |
| Less non-recognised deferred tax asset                                     | (11,116)               | -  | (649)                  | 5,435                                       | (6,330)                |
| <b>Total net deferred tax (liability)/assets</b>                           | <b>(9,494)</b>         | <b>(696)</b>                                       | <b>(812)</b>           | <b>(177)</b>                                | <b>(11,179)</b>        |

In the context of the Group's current structure, tax losses and current tax assets of the different companies may not be set off against current tax liabilities and taxable profits of other companies and, accordingly, taxes may accrue even where there is a net consolidated tax loss. Therefore, the deferred tax asset of one company of the Group is not offsetable against deferred tax liability of another company. As at 31 December 2004, a deferred tax asset in the amount of US\$10,833 (31 December 2003: US\$3,689 for continuing operations and US\$6,330 for entity) has not been recognised as it is not probable that sufficient taxable profit will be available to allow the benefit of that deferred tax asset to be utilised.

At 31 December 2004 the Group has not recognised a deferred tax liability in respect of US\$19,179 (US\$18,238 for continuing and for entity in 2003) of temporary differences associated with investments in subsidiaries as the Company is able to control the timing of the reversal of those temporary differences and does not intend to reverse them in the foreseeable future.

## 29. Provisions for liabilities and charges.

| Continuing operations                        | Provision<br>for loss-<br>making<br>contracts | Provision<br>for<br>warranties | Provision for<br>unused<br>vacations | Provision<br>for legal<br>claims | Provision<br>for spoilage | Other<br>provisions | TOTAL   |
|--|---|--------------------------------|--------------------------------------|----------------------------------|---------------------------|---------------------|---------|
| <b>At 31 December 2003</b>                   | -   | 636                            | 3,040                                | -                                | -                         | 2,116               | 5,792   |
| Additional reserve through Skoda acquisition | 4,663   | 3,875                          | 1,237                                | 797                              | 144                       | 1,360               | 12,076  |
| Charge for year                              | 533   | 1,856                          | 362                                  | 1,314                            | 1,493                     | 2,389               | 7,947   |
| Used during the year                         | (2,850)                                       | (571)                          | (1,772)                              | (215)                            | (94)                      | (1,394)             | (6,896) |
| Reversal of provision                        | -   | (2,796)                        | -                                    | -                                | -                         | (110)               | (2,906) |
| Disposal of non-core businesses              | -   | -                              | (210)                                | -                                | -                         | -                   | (210)   |
| Exchange differences                         | 580   | 476                            | 606                                  | 284                              | 200                       | 327                 | 2,581   |

**29. Provisions for liabilities and charges (continued)****Provision for loss-making contracts**

Provisions for expected losses on loss-making contracts are recognized when the expected revenues are lower than the expected costs to completion. It is expected that US\$2,935 will be used during 2005.

**Provision for warranties**

The Group gives warranties on certain products and undertakes to repair or replace items that fail to perform satisfactorily. A provision of US\$3,476 (2003: US\$636) has been recognised at the year-end for expected warranty claims based on past experience of the level of repairs and returns. It is expected that US\$2,058 will be used during 2005, and US\$1,418 during 2006.

**Provision for unused vacations**

Provision for unused vacations is recognized based on an individual analysis of the unused vacation per individual employees. The amount of US\$3,353 is expected to be used during 2005.

**Provision for legal claims**

The amounts shown comprise gross provisions in respect of certain legal claims brought against the Group by customers. The balance at 31 December 2004 of US\$2,180 is expected to be utilised during 2005. In the opinion of the directors, after taking appropriate legal advice, the outcome of these legal claims will not give rise to any significant loss beyond the amounts provided at 31 December 2004.

**Provision for spoilage**

Provision for spoilage is recognized when there is a significant probability of spoilage in the production of a new product. It is expected that US\$1,752 will be used during 2005.

All of these provisions are included in the balance sheet within other payables and accrued expenses (note 17).

**30. Contingencies, commitments and operating risks****Capital commitments**

As at December 31, 2004 the Group had contractual commitments for the purchase of property, plant and equipment from third parties for US\$2,354 (December 31, 2003: US\$2,702 for continuing operations and US\$2,702 for Entity).

**Taxation**

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

As at 31 December 2004 management believes that its interpretation of the relevant legislation is appropriate and the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued for in these financial statements.

In particular, management consider that there is a risk of the current classification of revenue from a certain contract to deliver equipment, processed by a Group company in Russia, to Syria as zero-rated for VAT purposes, based on its categorisation as a contract for "processing of goods", may be challenged following recent changes in the Customs Code. In the event of a challenge being successful, additional VAT of approximately US\$8 million could be payable.

**30. Contingencies, commitments and operating risks (continued)*****Insurance policies***

The Group insures all significant property and work-in-progress and shipments in relation to significant contracts. As at 31 December 2004, most of the Group's property is insured.

***Environmental matters***

The enforcement of environmental regulation in Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised immediately. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

***Legal proceedings***

During the year, the Group was involved in a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Group, and which have not been accrued or disclosed in these consolidated financial statements.

***Guarantees***

At 31 December 2004, the Group has guaranteed the following US dollar denominated loans issued:

| <b>Lender</b>          | <b>Borrower</b>        | <b>Amount of guarantee</b> | <b>Expiry date</b> |
|------------------------|------------------------|----------------------------|--------------------|
| OVK                    | Ural International     | 1,700                      | February 2005      |
| Citibank Romania S.A.  | UPET S.A.              | 1,021                      | May 2005           |
| Kokoda Product Carrier | Shipleigh Trading Ltd. | 1,860                      | January 2005       |
| Promtorgbank           | OMZ-Kran               | 627                        | March 2005         |
| VTB                    | OMZ-Kran               | 1,600                      | March 2006         |
| <b>Total</b>           |                        | <b>6,808</b>               |                    |

As at 31 December 2003, the Group guaranteed US dollar denominated bank loans totalling US\$3,300 issued to non-core business-units, sold in 2004.

The guarantee issued

At 31 December 2004, the Group has the following guarantees provided in favour of the Group:

| <b>Bank</b>                | <b>Customer</b>      | <b>Amount of guarantee</b> | <b>Expired date</b>   |
|----------------------------|----------------------|----------------------------|-----------------------|
| Gazprombank Moskva         | Severogazprom        | 123,332                    | January 2005          |
| Barclays Bank PLC (France) | Framatome, Schneider | 7,630                      | August 2005           |
| Komerční banka             | I and C Energo       | 5,133                      | August 2005           |
| ČSOB                       | Solar Turbines       | 1,876                      | November 2005         |
| Other                      | Other                | 9,920                      | August 2005-June 2007 |
| <b>Total</b>               |                      | <b>147,891</b>             |                       |

At 31 December 2004, Gazprombank provided the guarantee for Severogazprom in favour of the Group in amount of US\$123,332 as security of the letter of credit

At 31 December 2003 the amount of guarantees provided in favour of the group was US\$0.

**30. Contingencies, commitments and operating risks (continued)**

At 31 December 2004, the Group borrowings and fulfilment of contract obligations were secured by following third party guarantees:

| Customer/Creditor | Guarantor            | Amount of guarantee | Expired date          |
|-------------------|----------------------|---------------------|-----------------------|
| CHEZ              | Komerční banka       | 28,262              | August 2005           |
| ING Bank          | VTB                  | 3,290               | June 2005             |
| PAKS              | Bawag Bank CZ        | 1,859               | September 2005        |
| Severogazprom     | Česká exportní banka | 2,355               | November 2005         |
| Framatome S.A.    | Komerční banka       | 1,360               | October 2004          |
| Other             | Other                | 1,803               | January-November 2005 |
| <b>Total</b>      |                      | <b>38,929</b>       |                       |

At 31 December 2004, Komerční banka issued the guarantee in amount of US\$28,262 in favour of CHEZ to secure the fulfilment of ŠKODA JS a.s. obligations under SKŘ Dukovany contract.

**Operating environment of the Company**

Whilst there have been improvements in the economic situation in the Russian Federation in recent years, the country continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible in most countries outside of the Russian Federation, restrictive currency controls, and relatively high inflation.

The prospects for future economic stability in the Russian Federation are largely dependent upon the effectiveness of economic measures undertaken by the government, together with legal, regulatory, and political developments.

**31. Earnings per share**

Earnings per share is calculated by dividing the net income attributable to participating shareholders by the weighted average number of ordinary in issue during the period, excluding the average number of ordinary shares purchased by the Group and held as treasury shares (note 22).

**Basic earnings per share**

|   | 2004                  |                         |               | 2003                  |                         |               |
|---|-----------------------|-------------------------|---------------|-----------------------|-------------------------|---------------|
|   | Continuing operations | Discontinued operations | Entity        | Continuing operations | Discontinued operations | Entity        |
| Weighted average number of ordinary shares outstanding (thousands)      | 35,426                | 35,426                  | 35,426        | 35,350                | 35,350                  | 35,350        |
| Adjusted for weighted average number of treasury shares (thousands)     | (3,446)               | (3,446)                 | (3,446)       | (3,481)               | (3,481)                 | (3,481)       |
| Weighted average number of ordinary shares in issue (thousands)         | 31,980                | 31,980                  | 31,980        | 31,869                | 31,869                  | 31,869        |
| <b>Profit for the year attributable to the Company's equity holders</b> | <b>59,116</b>         | <b>4,398</b>            | <b>63,514</b> | <b>20,246</b>         | <b>4,737</b>            | <b>24,983</b> |
| <b>Basic earnings per share</b>   | <b>1.85</b>           | <b>0.14</b>             | <b>1.99</b>   | <b>0.64</b>           | <b>0.14</b>             | <b>0.78</b>   |

**31. Earnings per share (continued)****Diluted earnings per share**

Diluted earnings per share is calculated adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. During 2004 and 2003 the Company's only dilutive potential ordinary shares were share options.

|   | 2004                  |                         |               | 2003                  |                         |               |
|---|-----------------------|-------------------------|---------------|-----------------------|-------------------------|---------------|
|   | Continuing operations | Discontinued operations | Entity        | Continuing operations | Discontinued operations | Entity        |
| Weighted average number of ordinary shares in issue (thousands)                       | 31,980                | 31,980                  | 31,980        | 31,869                | 31,869                  | 31,869        |
| Weighted average number of share options outstanding (thousands)                      | -                     | -                       | -             | 881                   | 881                     | 881           |
| Weighted average number of dilutive shares (thousands)                                | 544                   | 544                     | 544           | 458                   | 458                     | 458           |
| Weighted average number of ordinary shares for diluted earnings per share (thousands) | 32,524                | 32,524                  | 32,524        | 33,208                | 33,208                  | 33,208        |
| <b>Profit for the year attributable to the Company's equity holders</b>               | <b>59,116</b>         | <b>4,398</b>            | <b>63,514</b> | <b>20,246</b>         | <b>4,737</b>            | <b>24,983</b> |
| <b>Diluted earnings per share</b>   | <b>1.82</b>           | <b>0.13</b>             | <b>1.95</b>   | <b>0.61</b>           | <b>0.14</b>             | <b>0.75</b>   |

**32. Principal subsidiaries**

The principal subsidiaries consolidated within the Group and the share in subsidiaries held by the Group are as follows:

| Entity  | Country of Incorporation | Activity  | 2004<br>% of share capital | 2003<br>% of share capital |
|---|--------------------------|---|----------------------------|----------------------------|
| OAO Izhorskiye Zavody ("Izhorskiye Zavody")         | Russia                   | Production of equipment for nuclear power plants and mining equipment | 80.1                       | 80.1                       |
| OAO Ural Heavy Machine-Building Plant ("Uralsmash") | Russia                   | Production of drilling, mining and metallurgical equipment            | 74.2                       | 74.2                       |
| OOO OMZ SpecStal ("SpecStal")                       | Russia                   | Production of specialty steels  | 100                        | 100                        |
| OOO OMZ Gornoe oborudovanie i tehnologii («GoiT»)   | Russia                   | Engineering and sales of mining equipment                             | 100                        | 100                        |
| ZAO Komplekt Atom Izhora                            | Russia                   | Engineering and installation of nuclear power plant equipment         | 100                        | 100                        |
| OOO OMZ Sibir                                       | Russia                   | Sales of mining equipment   | 100                        | 75                         |
| OOO OMZ   | Russia                   | Corporate services  | 100                        | 100                        |
| ŠKODA JS a.s.                                       | Czech Republic           | Production of equipment for nuclear power plants                      | 100                        | -                          |
| ŠKODA Hute  | Czech Republic           | Production of specialty steels  | 100                        | -                          |
| ŠKODA Kovarny                                       | Czech Republic           | Production of specialty steels  | 100                        | -                          |
| OMZ Morskie & Neftgazovye Proekty ("OMZ MNP") *     | Russia                   | Engineering and sales of oil and gas equipment and ships              | -                          | 100                        |
| OAO Krasnoe Sormovo Plant ("Krasnoe Sormovo") *     | Russia                   | Shipbuilding  | -                          | 61                         |
| OAO SF Almaz ("Almaz") *                            | Russia                   | Shipbuilding  | -                          | 72.8                       |
| OAO Volgograd shipbuilding plant*                   | Russia                   | Shipbuilding  | -                          | -                          |

**32. Principal subsidiaries (continued)**

| Entity   | Country of Incorporation | Activity   | 2004<br>% of share capital | 2003<br>% of share capital |
|--|--------------------------|--|----------------------------|----------------------------|
| OAo NPO Burovaya Tekhnika ("Burovaya Tekhnika") *                  | Russia                   | Production of drilling equipment, research and development for oil companies               | -                          | 56.8                       |
| ZKB Korall *   | Ukraine                  | Design and engineering of offshore oil drilling and production units                       | -                          | -                          |
| FGL Buyer, LLC *   | USA                      | Design and engineering of offshore oil drilling and production units                       | -                          | 75                         |
| Third International Shipbuilding Plant * S.C. UPET S.A. ("UPET") * | Russia<br>Romania        | Shipbuilding   | -                          | 73.9                       |
|  |                          | Production of mobile rings and components for offshore rigs and multi-purpose metal valves | -                          | 66                         |
| OAo Pavlovsky Machinery Plant ("Pavlovsky Machinery Plant") *      | Russia                   | Production of drilling equipment   | -                          | 90.8                       |
| OAo Zavod Nizhegorodskiy Teplokhod ("Nizhegorodskiy Teplokhod")    | Russia                   | Shipbuilding   | -                          | 55.7                       |
| OOO OMZ-Kran*  | Russia                   | Engineering and sales of handling equipment  |                            | 100                        |
| Shipley Trading Ltd.*  | British Virgin Islands   | Investing activities   |                            | 100                        |

\*-In 2004 these companies were sold to certain members of the management (see note 7).

**33. Financial risk management*****Credit risk***

Financial assets, which potentially subject the Group's entities to credit risk, consist principally of accounts receivable. The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. The carrying amount of accounts receivable, net of provision for impairment of receivables, represents the maximum amount exposed to credit risk. The Group has no significant concentrations of credit risk. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the provision already recorded.

***Foreign exchange risk***

The Group exports production to foreign countries and attracts substantial amount of foreign currency denominated long-term borrowings and is thus exposed to foreign exchange risk. Foreign currency denominated assets and liabilities give rise to foreign exchange exposure.

The Group does not have formal arrangements to mitigate foreign exchange risks of the Group's operations, except for the ŠKODA companies. However, management believes that the Group is secured from foreign exchange risks as foreign currency denominated sales are used to cover repayment of foreign currency denominated borrowings. ŠKODA companies apply the hedging of future cash flows, using financial derivative contracts.

***Interest rate risk***

The Group's income and operating cash flows are substantially independent of changes in market interest rates. The Group is exposed to interest rate risk through market value fluctuations of interest-bearing long-term borrowings. The majority of interest rates on long-term borrowings are fixed, these are disclosed in note 18. The Group has no significant interest-bearing assets.

**34. Post balance sheet events*****Sale of Zarubezhenergoproekt.***